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(9:05 a.m.)
JANUARY 15, 2013
CHAIRMAN:
Q. Before we start, I think there's a preliminary matter we got to deal with, Madam Solicitor.
MS. GLYNN:
Q. It's just a housekeeping item, Mr. Chairman. Order No. PU 43 2009, which is the last GRA Order, we are going to enter that as a consent exhibit.
CHAIRMAN:
Q. I believe we're back to Madam Perry, Mr. Kelly, and I believe you are in charge.
KELLY, Q.C.:
Q. Thank you, Mr. Chairman.
CHAIRMAN:
Q. Insofar as anybody is ever in charge.
MS. JOCELYN PERRY - EXAMINATION BY KELLY, Q.C.:
Q. I assume I only speak for this piece. Ultimately, the control is in the Board. Mr. Chairman, there were a couple of questions that arose the last day with respect to executive compensation, so before I turn Ms. Perry over for cross-examination, I'm just going to go back and deal with those couple of

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questions. Ms. Perry, I understand you are the Vice President at Newfoundland Power who has responsibility for human resource matters?
MS. PERRY:
A. Yes, I am.
KELLY, Q.C.:
Q. And you're familiar with the structure of the company's executive compensation program?
MS. PERRY:
A. Yes, it's part of my responsibility to prepare the materials for Newfoundland Power's Board of Directors, which relate to compensation for the company's executive.
KELLY, Q.C.:
Q. Now there was a question from the consumer advocate. We'll find it on page 82 at lines 6 to 13 of the transcript, and Mr. Ludlow was asked - page 82, if you'll go down a little bit further. There you go. Mr. Ludlow was asked by the consumer advocate what it would mean in terms of extra compensation for executives and managers if the Board were to allow the 10.4 percent return on equity proposed by Newfoundland Power in this Application. Can you address that question?

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MS. PERRY:
A. Yes, I can. No executive or manager would earn anything more if the return on equity was set at 10.4 percent. Newfoundland Power's senior management salaries and benefits are established relative to market benchmarks. These benchmarks do not consider the company's allowed or earned returns on equity. The only part of Newfoundland Power's senior management compensation program which relates to return on equity is the earnings target used for the short term incentive for the STI planned. The earnings target used for STI purposes by the company has always reflected the regulated return on equity approved from time to time by this Board. If Newfoundland Power achieves the regulated return on equity approved by the Board, then its executives and managers will achieve 100 percent of the target for earnings within the STI program. Establishing the return on equity target for the STI plan to reflect the return on equity approved by the Board recognizes that the return on equity allowed by the Board by regulatory purposes is not a guaranteed return. The earnings target

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in the STI plan exists to incent senior management to achieve the return on equity approved by the Board for rate making purposes. So if this Board approved Newfoundland Power's proposed return on equity of 10.4 percent for 2013, the company's STI earnings target will reflect a regulated return on equity of 10.4 percent for 2013. If the company earns 10.4 percent return on equity, then the STI plan would indicate that 100 percent of the earnings target has been met. If on the other hand, the Board allows a return on equity for 2013 of 9.5 percent, then the earnings STI earnings target will reflect a return on equity of 9.5 percent. If the company earns 9.5 percent for 2013, then the STI plan would indicate that 100 percent of the earnings target has been met. Since the earnings target used in the STI plan reflects a return on equity approved by the Board for regulatory purposes, senior management will be no better or worse off if the Board were to establish a return on equity for rate making purposes of 10.4 percent, or some other amount. The Board permits only the target STI

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plan amount to be included in the revenue requirement. Any amounts paid in excess of STI targets are effectively funded by the shareholder.

KELLY, Q.C.:

Q. Okay. Now next there was a question or a discussion that took place with the Chair of the Board. If we go to page 141, Chris, at line 23 - there we go. There was a discussion with Mr. Ludlow about the amount of executive compensation which was paid for by the rate payers of Newfoundland Power. Do rate payers fund the total compensation paid to Newfoundland Power executives?

MS. PERRY:

A. No, they do not. At Newfoundland Power's last general rate hearing in 2009, Karl Aboud of HAY Group indicated that the company's total compensation included four key components. That would be the salary, STI, long term incentives, and benefits. It is Newfoundland Power's total compensation which is benchmarked to the 50th percentile of the Canadian commercial industrial group. Newfoundland Power's rate payers have never

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paid the cost of Newfoundland Power's executive's long term incentives. The cost of these incentives which are in the form of options to buy common shares of Fortis Inc., are borne by Fortis Inc. In 2011, the value of these stock options were approximately 160,000 for Mr. Ludlow, 53,000 for Mr. Smith, and 48,000 for each of myself and Mr. Alteen. Given that Fortis Inc. contributes to this extent, it is clear that the company's rate payers do not fund the total compensation paid to Newfoundland Power's executives. This level of shareholder contributions to executive compensation is consistent with that which has existed for Newfoundland Power for well over a decade.

KELLY, Q.C.:

Q. Thank you, Ms. Perry. Does that conclude your additional testimony?

MS. PERRY:

A. Yes, it does.

CHAIRMAN:

Q. But those were dollars, not shares?

MS. PERRY:

A. That's dollars, that's dollars.

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CHAIRMAN:

Q. Okay.

MS. PERRY:

A. As the value of the stock options.

CHAIRMAN:

Q. Sure, okay.

KELLY, Q.C.:

Q. Thank you, Mr. Chairman. The witness is available for cross-examination.

CHAIRMAN:

Q. Mr. Johnson, sir.

MS. JOCELYN PERRY - EXAMINATION BY MR. JOHNSON:

MR. JOHNSON:

Q. Ms. Perry, Newfoundland Power, I'm sure you're aware, would have to go back quite a while over its books to find a year where it did not earn its allowed return, correct?

MS. PERRY:

A. I think that's a fair statement, yes.

MR. JOHNSON:

Q. And I believe 1995, some 17/18 years ago would have been the last year, is that correct?

MS. PERRY:

A. I'd have to check that, but around that time.

MR. JOHNSON:

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Q. Around that time, and just to - if we could pull up CA-NP-381, in that regard. In this question the company was asked in part, (a) to provide the allowed ROE and actual ROE earned by Newfoundland Power since 1990. I take it you probably would have had a hand in preparing this response?

MS. PERRY:

A. Yes, I've seen this response.

MR. JOHNSON:

Q. Can you confirm for the record that this would indicate that in each and every year since 1996, Newfoundland Power has earned greater than its allowed ROE?

MS. PERRY:

A. I can confirm that Newfoundland Power has earned within its allowed range of return, yes, since 1995.

MR. JOHNSON:

Q. Okay, but there is an actual - there's an allowed and an actual column, and would you - you wouldn't take exception that since 1996 the actual ROE has been in excess of the allowed ROE because it's stated there and it's obvious?

MS. PERRY:
A. Yes, I would agree. I'm just saying that - but the actual ROE's are within the allowed range of return for Newfoundland Power.
MR. JOHNSON:
Q. Right, and if we could turn up Grant Thornton's report, the financial consultant's report that was prepared for the Board and reviewed this Application. I believe that would be Consent # 2, in particular, page 19.
MS. GLYNN:
Q. If you'll go under the Board expert evidence, Chris, expert evidence for - there you go. What was the page reference again, Tom, Mr. Johnson?
MR. JOHNSON:
Q. Page 19.
MR. KIRBY:
Q. 19.
(9:15 a.m.)
MR. JOHNSON:
Q. And just scroll down a little bit further. I'm just bringing your attention to the section on return on rate base, lines 21 to 28, and in particular the chart which shows

the actual return on average rate base, the upper end of the range set by the Board, the lower end of the range, and so since this Board heard the last GRA in 2009, the company has earned above the midpoint of the range of return on rate base in 2010, right?
MS. PERRY:
A. Yes, that is correct.
MR. JOHNSON:
Q. And they earned - the company earned to the upper limit in 2011?
MS. PERRY:
A. That is correct.
MR. JOHNSON:
Q. So 8.14 in a range of 7.78 to 8.14, and the company's expected to earn again within the range in 2012?
MS. PERRY:
A. Yes, that is correct.
MR. JOHNSON:
Q. And, Ms. Perry, would you agree with me that Newfoundland Power's proposed 2013 and 2014 return on equity of 10.4 and 10.5 are out of line with the spreads between Newfoundland Power's return on equity and return on rate

base over the last several years?
MS. PERRY:
A. I'm not sure I understand your question, Mr. Johnson.
MR. JOHNSON:
Q. If we could go to page 21 of the Grant Thornton report. Grant Thornton - if we could go even a little bit further, so we can see the years on the bottom. Grant Thornton has graphed - provides a graphic illustration on the return on average common equity and average rate base over the period from 2007 to 2014?
MS. PERRY:
A. Yes, I see that.
MR. JOHNSON:
Q. And what I'm bringing your attention to, and for those who are looking at the computer generated, is that the pink line is the return on average rate base and the blue line is the return on average common equity. The proposition I'm putting to you is that your proposed or your company's proposed ROE for 2013 and 2014 are out of line with the spreads that we have seen over the last - well, to

2007 in this table. Would you agree with that?
MS. PERRY:
A. I will agree that the difference is more. However, the 2013 and 2014 is based on the proposed 10.4 that we've put forward in this Application. I mean, every so many number of years Newfoundland Power evaluates all their costs and cost of capital is one of those costs that we evaluate.
MR. JOHNSON:
Q. But there'd be no doubt that if this Board were to accede to the company's request of a 10.4 percent return on common equity in 2013 and higher again in 2014, that this would be the result of the spreads between the return on rate base and return on equity?
MS. PERRY:
A. Yes, that is correct.
MR. JOHNSON:
Q. And based on this graphic presentation, if that result were to happen, it would produce an anomalous result relative to what we've seen since 2007?
MS. PERRY:

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A. I'm not sure I'd describe it as such. It's a factor of how out rate base is growing and the mathematical difference, shall I say, between rate of return on rate base and return on average common equity, but, you know, what we are here to deliberate is a fair and reasonable return on equity for Newfoundland Power and what that translates into a return on rate base, it will fall out from that.

MR. JOHNSON:

Q. Ms. Perry, the 10.4 percent request, and 10.5 percent for 2014, you'll acknowledge that would be the highest in Canada. If you were given that, that would be the highest, right, for a regulated utility?

MS. PERRY:

A. I believe so, and I would like to make a correction. The proposal was 10.4 percent for both 2013 and 2014.

MR. JOHNSON:

Q. Okay, and Mr. Ludlow, in his evidence indicated that - he stated that the ROE must be fair to Newfoundland Power and to the customer. You were here when he said that?

MS. PERRY:

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A. Yes, I was.

MR. JOHNSON:

Q. And I would like for you to fully explain how a request to have 10.4 percent return on equity, being the highest in the country, fully explain how that request should be considered to be fair for your customers?

MS. PERRY:

A. Mr. Chairman, as I said earlier, we go through this process every few years where we evaluate the cost of capital for Newfoundland Power, and evidence is brought before this Board by expert witnesses that lay out an appropriate and fair return for Newfoundland Power. We've engaged two experts. Both experts have indicated that the range of return is 10.4 or 10.5. The 10.4, yes, I appreciate that it may be the highest. When we look across the country, I do look at Fortis BC, they're currently at 9.9 percent, and certainly the 10.4 percent does set Newfoundland Power up with respect to its financial matrix and its financial profile, such that the credit ratings that fall from it simply support the rating that we have today. So I think that

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the proposal that we've put forth has been put forth from expert witnesses, and it's in line with maintaining Newfoundland Power's financial integrity, and that's good for customers.

MR. JOHNSON:

Q. Okay, and so part of it is driven - part of the fairness equation is driven by the fact that your expert witnesses have recommended the number, I take it?

MS. PERRY:

A. Certainly, yes.

MR. JOHNSON:

Q. And part of it is driven by the fact that you think it puts you - well, in fact, in excess of where Fortis BC is?

MS. PERRY:

A. No, the proposal was based certainly on the expert's proposal. That's first and foremost.

MR. JOHNSON:

Q. Okay, and what's the tie in to Fortis BC then?

MS. PERRY:

A. I'm simply saying that if I had to look across the country and look at what other distribution electric utilities are earning,

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and other distribution companies across Canada, I'm saying that there's one utility in British Columbia that's currently earning 9.9 percent.

MR. JOHNSON:

Q. And you were here yesterday, and I understand that Ms. McShane confirmed that that company is not a distribution company, but it's a vertically integrated company?

MS. PERRY:

A. Fortis BC Energy or Fortis BC Electric?

MR. JOHNSON:

Q. Fortis BC Electric.

MS. PERRY:

A. Yes.

MR. JOHNSON:

Q. Is that the 9.9 that you're referring to?

MS. PERRY:

A. Yes.

MR. JOHNSON:

Q. Yeah, and that's a vertically integrated company?

MS. PERRY:

A. I believe so, yes.

MR. JOHNSON:

Q. And in your mind, would it be relevant for the Board to consider the difference between a vertically integrated company and a distribution poles and wires company like Newfoundland Power?

MS. PERRY:

A. I look at this pretty simplistically when I compare Newfoundland Power to other businesses across Canada. I mean, I'd look at Fortis BC Electric, and they're a regulated utility, they have regulated assets, they are similar - well, they are bigger than us. They have cost of service regulation, they have reserve mechanisms, such as Newfoundland Power, so I evaluate companies on that basis. I'll leave it up to Ms. McShane and Dr. Vander Weide with respect to comparable companies to include for comparison of fair returns for Newfoundland Power.

MR. JOHNSON:

Q. So when Newfoundland Power states in its reply to one of the PUB's staff question about who you compare it to, did you have a hand in preparing that response?

MS. PERRY:

A. Yes, I'm familiar with that response, yes.

MR. JOHNSON:

Q. And when you said that Newfoundland Power would be comparable with Fortis BC, you want to be very clear that you're only saying that because you're both regulated utilities, you both are under cost of service, but it was a pretty high level assessment?

MS. PERRY:

A. And it would be, Mr. Chairman. I mean, I'm not privy to all of the operational day to day runnings of Fortis BC, so, yes, it is at a high level.

MR. JOHNSON:

Q. And in terms of your reference to what 10.4 percent would do to your company's matrix, credit matrix, etc., you would confirm that that would bring your matrix up quite considerably higher than what they are in 2012, for instance?

MS. PERRY:

A. Well, if I - if we turn to Exhibit - I'll get the exhibit number.

MR. JOHNSON:

Q. Three?

MS. PERRY:

A. Exhibit 6, and Exhibit 3, I guess, we'll need two of them. If you look at Exhibit 6 and you look at lines 34, 35, and 36, under the proposed for 2013, you'll see that the interest coverage is 2.6, and that would be up from 2.3 in 2012.

MR. JOHNSON:

Q. Uh-hm.

MS. PERRY:

A. You'll see the CFO to interest to be 3.6 times. This is up from 3.2. Then you'll see the CFO to debt percentage to be 18.3, and that's up from 15.7.

MR. JOHNSON:

Q. Uh-hm.

MS. PERRY:

A. And then you'll notice that they're somewhat similar, but slight decrease in the CFO to debt as you go out into 2014 down to 16.4, over in the last column. When I look at the proposed matrix here, Moody's has indicated that the CFO to interest range should be in the low 3's. So the proposal is 3.4 - 3.6 and 3.4.

MR. JOHNSON:

Q. Uh-hm.

MS. PERRY:

A. And CFO to debt, the range that they provide is 15 to 17, and I see here that by the end of 2014, we'll be at 16.4. So we're within the ranges that -

MR. JOHNSON:

Q. And I intend to have a discussion with you about Moody's, but my point is you have spoken about part of the reason why a rate payer would consider your request on equity fair is because of its impact on financial matrix and financial integrity of the company, but, Ms. Perry, it's beyond dispute, is it not, that over the period from 2007, 2008, 2009, 2010, 2011, that the financial integrity of Newfoundland Power has been very much intact, correct?

MS. PERRY:

A. Yes, it has, I would confirm that.

MR. JOHNSON:

Q. At significantly lower ROEs than what you're putting forward in this case?

MS. PERRY:

A. Yes, I would agree that the financial integrity has been maintained. Certainly during the last rate case, there were concerns about our decreasing matrix in the 2009 hearing, and coming out of that hearing the matrix that you see in 2010, if you go to Exhibit 3 - so if you go down to lines 37, 38, and 39, you will note that - and 2010 is a good reflection of how we were set up, I guess, from a financial matrix perspective coming out of the last rate case, and so the interest coverage was 2.4, the CFO to interest was 3.4, and the CFO to debt was 17.6. So those matrix itself is not materially different than the matrix that we're proposing here in this Application.

MR. JOHNSON:

Q. But Ms. Perry, you're aware that return on equity has got to be fair to equity holder, and you're well familiar with the proposition that we don't key off a fair return on equity to a particular matrix, do we?

MS. PERRY:

A. That is true, yes.

MR. JOHNSON:

Q. In fact, it would be not appropriate, would it, to tie or allow ourselves to determine what a fair ROE was by what a particular credit matrix would result from that ROE?

MS. PERRY:

A. I disagree with that concept. I think that one of the requirements of a fair return is that it should maintain a company's financial integrity. So I think while debt rating agencies are not going to come out and say what a fair return should be for an equity holder, the return does matter to the matrix. The matrix matter to the financial integrity and that is one of the requirements of a fair return.

(9:30 a.m.)

MR. JOHNSON:

Q. Let's put it this way, Ms. Perry, if for the sake of argument we could conclude that a return based on Newfoundland Power's profile as compared to a company that has a similar profile that we wouldn't have to make all sorts of adjustments to, if we could say an equity investor in this company deserves 8 percent, and they deserve 8 percent in that

one, would we - would we then do an extra step and say, oh, yes, but, you know, we really have to adjust Newfoundland Power's 8 which would be fair to the equity investor, we'd have to adjust that up because we've got to cover off these matrix. That's not your proposition, is it?

MS. PERRY:

A. My understanding, Mr. Chairman, is that one of the requirements of a fair return is that it should maintain the company's financial integrity, and if it was felt that the financial matrix of Newfoundland Power were not sufficient to maintain that, then I think the two are connected.

MR. JOHNSON:

Q. And would - under that logic, though, would the equity holder in Newfoundland Power be better off than they really ought to be, would they? Wouldn't that follow, because you're saying to the equity investor in Newfoundland Power, look, if we're looking at two equal companies that we don't have to make adjustments to, and you deserve 8, but, you know, we've got to do something with the

financial matrix, so we're going to give you more, is that the proper response?

MS. PERRY:

A. I think it is.

MR. JOHNSON:

Q. Okay.

MS. PERRY:

A. In the fact that if Newfoundland Power were to jeopardize its financial integrity, and let's just say be downgraded, that in essence will cost consumers a lot more and it certainly - I can't see how that would benefit the company or the customers in the long run, and again - now unless I'm mistaken, my understanding is that one of the requirements of a fair return is that it should maintain a company's financial integrity.

MR. JOHNSON:

Q. Yes, but isn't one of the other principles of a fair return that the return be comparable to an equal risk company, or to an investment that you can get in a comparable investment? Isn't that part of the fair return too?

MS. PERRY:

A. Certainly it is, but I think they are related,

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they come together. There's more than one requirement of a fair return, from what I understand.

MR. JOHNSON:

Q. And I'm aware of that, but what I'm trying to dial in on, is it Newfoundland Power's proposition that we might have to tinker upward with what would otherwise be considered a fair return on common equity in order to meet a credit matrix, in order to preserve the financial integrity, and if so, would that not give an equity investor in Newfoundland Power an advantage or a benefit over an investor - a common equity investor in a like company?

MS. PERRY:

A. I'm disagreeing with, I guess, the concept that - I think the two go hand in hand. If the utility is awarded a fair return, it should preserve its financial integrity. I mean, I don't know of a situation where at the end of the day - if a return was issued and 7.5 percent was viewed as a fair return as Dr. Booth's proposal is, and the financial matrix were below that indicated by Moody's as acceptable, once that order were granted by

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the Board, we would have to take a hard look at that because we're not preserving the financial integrity of Newfoundland Power, and for me the two would have to go hand in hand.

MR. JOHNSON:

Q. Well, let's flip it the other way then. What if we said all Moody's requires is "x" in terms of cashflow, interest coverage, and the other matrix, and if we arrived at a return on equity that produced - that covered us off in terms of what Moody's was concerned about, well, then that might mean that equity investors in Newfoundland Power could live with a lot less than what they're asking for. Would that be fair?

MS. PERRY:

A. No, that would not be fair.

MR. JOHNSON:

Q. Okay, because I thought I was just asking you the corollary of that.

MS. PERRY:

A. No, I guess - so I can explain, I believe that a utility is entitled to a fair return, and that fair return should maintain the financial integrity of the company, and it should be a

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consideration of the determination of a fair return.

MR. JOHNSON:

Q. Okay, but you would not consider, I take it, that it would be appropriate for an equity investor in Newfoundland Power to get a return over and above what an equity investor in a comparable risk enterprise should get just by merit of the fact that we've got to concern ourselves with credit matrix for Newfoundland Power?

MS. PERRY:

A. I think it's a fair observation that a utility with similar risk, an equity holder should get a return on comparable risk utilities, yes, but if the return is in some way jeopardizing the financial integrity of the company, I think it all has to be considered in the determination of a fair return.

MR. JOHNSON:

Q. I'm going to move on, but I just need to really understand this point, would you ever suggest, though, that if this Board were satisfied that, say, 7 percent is a fair return on common equity for Newfoundland

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Power, would they ever - should they ever entertain, in your view, giving you, say, 8 percent or maybe 8.5 if it preserved what you would term as the financial integrity of the company?

MS. PERRY:

A. I think it's one of the standards of a fair return standard that it should maintain the financial integrity of Newfoundland Power and it should be a consideration, yes.

MR. JOHNSON:

Q. So never mind a consideration, you would suggest that if it was necessary to preserve financial integrity, that an equity investor who otherwise would be entitled to 7, should probably get 8 or 8.5?

MS. PERRY:

A. Yes, I do.

MR. JOHNSON:

Q. Okay. I just need to understand your position on the point. We heard yesterday from Ms. McShane that she regards that the cost of equity for Newfoundland Power has declined from the last General Rate Application. You've heard that evidence?

MS. PERRY:
A. Yes, I did.
MR. JOHNSON:
Q. And you indicated that you hire advisors and experts, etc., so I expect that you accept that judgment?
MS. PERRY:
A. Yes, I respect the expert's opinion, yes.
MR. JOHNSON:
Q. And the 9 percent return that Newfoundland Power earned or was allowed in its 2010 GRA, was that a fair and just return? You just brought us through the table which indicated that it improved matrix and that sort of thing. Was that a fair and just return for Newfoundland Power?
MS. PERRY:
A. Well, the Board decides on what a fair return is for Newfoundland Power, and the way I see it simply is that once the evidence has been heard, and I respect that there's evidence brought forward on both sides to deliberate the cost of capital issue. Once that's done, the Board determines and orders what they deem to be a fair and reasonable return for

Newfoundland Power. Newfoundland Power has to evaluate the order in its entirety, and I guess, fundamentally, we have only a couple of choices, which is to accept the return, which is what we've done, or object, and in that case we accepted, but in terms of what is deemed to be fair, I'm going to let the Board hear the evidence and decide what an appropriate return is.
MR. JOHNSON:
Q. I understand, obviously, that's the province of the Board, but does Newfoundland Power have an opinion as to a judgment as to whether its return that was allowed the last time in 2009 GRA was fair?
MS. PERRY:
A. No, Mr. Chairman, I don't feel I can make that observation. I think that we accepted the return that was ordered by the Board. We presented evidence and the consumer advocate presented evidence on cost of capital, and the Board decides what an appropriate and fair return is for Newfoundland Power, and we accepted the Board's Order at that time.
MR. JOHNSON:

Q. So is it a matter of principle that you cannot say whether a return would be fair?
MS. PERRY:
A. Mr. Chairman, I'm certainly not a cost of capital expert and that was validated for me yesterday. However, again I look at it very simplistically. I'll look across the country, I'll look around North America and just see other returns. We'll all guilty of looking over our shoulder. That's certainly not how a fair return is determined, but it's certainly a way that I will evaluate the reasonableness of the order that we've been granted, and 9 percent was - at that particular time we accepted it. When we moved into 2011 and the return dropped to 8.38 and it was the lowest in the country, I tend to make more of a grand statement that that's not a fair return based on my simplistic view of looking across the country, that we were the lowest actually in North America, but I do leave the ultimate decision of a fair return up to the Board.
MR. JOHNSON:
Q. So would it be fair to - because I think you indicated, although it's not in your company

evidence, the written company evidence that you are sponsoring, there's no reference, Ms. Perry, in the written evidence to Newfoundland Power's submission, I don't believe, in your Application that the 8.38 which would have been the return on common equity permitted by the formula, that that was unfair. There's no reference in the Application to that, is there? I didn't see it.
MS. PERRY:
A. I believe the 8.38 was deemed not to be - I'd have to check that, Mr. Johnson.
MR. JOHNSON:
Q. If I could bring you to page 338. It starts on 337. In the concluding section, it says - are you there?
MS. PERRY:
A. Yes, I am.
MR. JOHNSON:
Q. "Section 80 of the Act entitles Newfoundland Power to reasonable opportunity to earn a just and reasonable return each year", and each year is in italics, "and in the Order PU-43 of 2009, the Board ordered continued use of the formula, as it believed financial market

conditions appear to be settling. The 8.38 percent estimated cost of equity indicated by the formula for 2011 was the result of declining forecast long Canada Bond yields. It was also the lowest rate making return on equity awarded for a Canadian investor owned utility in 2011. The estimated cost of equity of 7.85 percent indicated by the formula for 2012 did not constitute a fair return for Newfoundland Power. The August, 2012 consensus forecast indication of an estimated cost of equity of 7.53 percent for 2013 does not constitute a fair return for Newfoundland Power. Both are well below current rate making returns on equity for Canadian investor owned electric utilities". So while I see Newfoundland Power it its Application calling what was coming in by reason of the formula of 7.85 and 7.53 unfair, I didn't see you stating in your Application that the 8.38 was unfair.

MS. PERRY:

A. I'm recalling that in my opening last Thursday that I did indicate at that time that I believed in my opinion that the 8.38 was not a fair return.

MR. JOHNSON:

Q. And this is precisely why I'm bringing you here because was - when you said that, and it was also said that you were sponsoring the testimony in this section of the Application, the finance section, where I didn't see that statement, I was - I had to ask you about it. So did you prepare this section?

MS. PERRY:

A. Yes, I did, I had a hand in it, yes.

(9:45 a.m.)

MR. JOHNSON:

Q. A hand in it, and was there a reason why it was not stated in this that 8.38 was unfair?

MS. PERRY:

A. Well, for 2012 and 2013, Mr. Chairman, we have expert opinions which are indicating that the fair return for Newfoundland Power is something significantly above the 7.85 and the 7.53, and also it's not in line with maintaining our financial integrity. So that one, I will agree, is a bit easier with respect to making the statement of a fair return. In my opening, I believe the exact words I used was, "The 8.38 didn't appear fair

to me". We didn't have an expert opinion, but it didn't appear fair, given it was the lowest ROE in the country.

MR. JOHNSON:

Q. In the transcript, if we go there, it's at 154, I believe, page 154, you were asked a question - it's at the bottom of page 153. The question is, "In 2011, the formula indicated an estimated return on equity of 8.38 percent. Why didn't Newfoundland Power seek to suspend the operation of the formula for 2011". The answer, "Well, first of all, Newfoundland Power did not think the 8.38 percent return on equity in 2011 was a fair return. It was significantly lower than the returns of other investor owned utilities", you said, and I was just - again that statement is not made in the company's evidence that you're formally sponsoring.

MS. PERRY:

A. I would have to confirm, but I'm not sure that it is.

MR. JOHNSON:

Q. Okay. So is it the company's position now that 8.38 is fair - is unfair?

MS. PERRY:

A. Yes, that's the company's position, Mr. Chairman.

MR. JOHNSON:

Q. Okay, and what made it unfair?

MS. PERRY:

A. As I said earlier, Mr. Chairman, we did not have expert advice to tell us what a fair return was for 2011, but as a matter of principle, when I looked across the country and we were the lowest in the country, as I said, it didn't appear fair to me. I'm not a cost of capital expert, but it didn't appear fair to us, and what we were addressing in the opening was if it didn't appear fair and we didn't think it was fair, why did we not file at that time, and that's what I laid out in evidence as to why we decided not to file at that time.

MR. JOHNSON:

Q. Okay. Well, certainly - but certainly we know this about your assertion that the 8.38 percent wasn't fair, that assessment was not borne out of any evidence or expert analysis that Newfoundland Power availed of, that was

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more along the line of compared to others, correct?
MS. PERRY:
A. That's exactly what I said, yes.
MR. JOHNSON:
Q. Okay. Mr. Ludlow indicated at page 45 of the transcript - I'm just looking for it now. I was asking him that question at line 10, "And just to be clear, in 2001, when the company made - just made slightly more than what you are projected to make in 2012, that was a fair return in 2011 and preserved the financial integrity of the company", and Mr. Ludlow answers, "2011", and I say, "Yes", and he said, "Our return as stated, as I said earlier, was whatever I - what we were saying earlier, it was reasonable at that point in time, yes". So you're drawing a distinction between the allowed and what was achieved, but you would consider what Mr. Ludlow said to be accurate, that what was earned in 2011 was reasonable and fair?
MS. PERRY:
A. I'm not sure that's what Mr. Ludlow meant by that. I believe it had to do with preserving

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the financial integrity of the company.
MR. JOHNSON:
Q. Could I turn you to page 41. The question I asked Mr. Ludlow right after saying good morning to him, "You talked in your direct with Mr. Kelly about Newfoundland Power's returns over the last few years since the rate case, but I take it that you would confirm, Mr. Ludlow, would you not, that Newfoundland Power itself believes that its financial performance since the last general rate Application through to 2012 has been absolutely consistent with the company's financial integrity", and Mr. Ludlow says, "I would agree, Mr. Chairman, that we have performed very well in the past two or three years and it has not had a negative impact on the financial integrity of the company". I took it to mean in 2011 you performed very well.
MS. PERRY:
A. I would agree that Mr. Ludlow's response is agreeing that the financial performance in 2011 is consistent with maintaining the financial integrity of the company.

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MR. JOHNSON:
Q. He says, "We have performed very well in the past two or three years, and it has not had any negative impact". So is there a distance between you and Mr. Ludlow on this point?
MS. PERRY:
A. No -
MR. JOHNSON:
Q. He seems to be saying that the 2011 results were good. He characterized 2011, "We performed very well".
MS. PERRY:
A. Mr. Chairman, I would interpret, and I'm not one to speak for Mr. Ludlow, so - but in terms of how I would interpret this, "We performed very well", we did perform very well. We had an allowed return in 2011 of 8.38, and we earned at the top of our range that year, yes. So I would take that as meaning we performed very well in that particular year. That doesn't necessarily translate to me that we agreed it was necessarily a fair return that we were starting with, which was 8.38.
MR. JOHNSON:
Q. Okay. You were here when Ms. McShane

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testified yesterday. Could you indicate, you're the CFO, about financing flotation costs - could you fill us in, or fill me in at least, on that concept?
MS. PERRY:
A. Well, I think I would be out of step if I tried to interpret the adjustments that are made to Ms. McShane's or Dr. Vander Weide's cost of equity flotation costs, and I understand both of them are different for various reasons, but Ms. McShane explains what the flotation costs are in her evidence, and I'm not comfortable speaking to the nature of those costs.
MR. JOHNSON:
Q. So you're not in a position to say whether flotation costs are higher than they were in 2009, for instance?
MS. PERRY:
A. In simply comparing Ms. McShane's evidence?
MR. JOHNSON:
Q. Well, I was just interested generally about this flotation cost that gets referred to, and you can't offer anything on that?
MS. PERRY:

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A. No, I cannot.
MR. JOHNSON:
Q. Okay. Could I refer you to page 315 of the materials of the company, Ms. Perry, and at line 20, the company states that, "Risk is an assessment of the capability of an enterprise to recover its investment, as well as earn a return on that investment, and for regulated utilities such as Newfoundland Power, risk is generally considered to have business regulatory and financial elements", and the first line about the capability of an enterprise to recover its investment as well as earn a return on that investment, Dr. Booth, my expert witness, he says - he defines risk as the probability of incurring harm and he interprets this in the short run as failing to earn the allowed ROE, and the long run risk has the uncertainty of recovering the shareholder's investment in rape base. Would you accept that description as being reasonable?
MS. PERRY:
A. I think I would look at the ability to earn a return on the investment and to recover the

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investment both as long term risk, because once you invest in a company such as Newfoundland Power, you are into it for the long term. So I think I see it both as long term.
MR. JOHNSON:
Q. But surely what Dr. Booth defines as the probability of incurring harm in the short run as failing to earn the allowed ROE, that would be risk, right?
MS. PERRY:
A. Certainly.
MR. JOHNSON:
Q. And that would be not long term risk, that would be short term risk, wouldn't it?
MS. PERRY:
A. I guess it depends, Mr. Chairman, how you're looking at it. I look at the risk from an equity perspective. If they're investing the company, they're into it for the long haul and so I look at the risk of earning a return each and every year.
MR. JOHNSON:
Q. And that's my point. Each and every year, you know, there's -- the investor, equity investor

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asks him or herself "did I earn the allowed ROE?" and that's made on an annual -- that's an annual determination.
MS. PERRY:
A. Yes, I believe it is.
MR. JOHNSON:
Q. Right, and we've -
MS. PERRY:
A. But I will qualify that you don't make investment decisions based on your ability to only earn within one year.
MR. JOHNSON:
Q. No, no, but let's put it this way, as we've seen from the earlier RFI reply this morning, going back to, I think it was 1996, Newfoundland Power has never failed to earn its allowed ROE, right?
MS. PERRY:
A. That's correct.
MR. JOHNSON:
Q. And would that demonstrate to you Newfoundland Power's low risk nature?
MS. PERRY:
A. No. I would make the observation that Newfoundland Power has made -- earned within

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its allowed range of return, which tells me that there's a couple of things happening. One is that we are set up appropriately as a utility with a reasonable opportunity to earn our return and secondly, that we're actually executing upon how we're structured and we're actually earning our return, because there's one thing to be provided the opportunity to earn the return and then there's the other thing of actually earning a return. So I think in general, utilities are considered low risk and I would consider that Newfoundland Power is very comparable to other utilities in our structure.
MR. JOHNSON:
Q. In terms of the set-up appropriately to be given a reasonable opportunity, what are you referring to in that regard?
MS. PERRY:
A. Mr. Chairman, I think that's everything from timeliness of Board orders to regulatory mechanisms that allow us to recover prudently incurred costs between test years that sets us up from a regulatory efficiency point of view and just it provides Newfoundland Power with

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that opportunity to earn a fair and reasonable return, which is good for Newfoundland Power and certainly good for Newfoundland Power's customers.

MR. JOHNSON:

Q. So these types of things are significant risk mitigators obviously, these accounts, for instance, the ability to have timely recoveries?

MS. PERRY:

A. I will agree that regulatory mechanisms that permit timeliness of recovery reduces the exposure to those cost variances, but risk is a relative concept which we've displayed in our evidence, and relative to other utilities they're very common, they're very consistent. What I will say is that not all reserve mechanisms that we have is just simply about risk reduction of Newfoundland Power. We actually have an excess earnings account which is simply solely about Newfoundland Power's return, not risk.

(10:00 a.m.)

MR. JOHNSON:

Q. And we'll talk about some of your accounts,

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but given Newfoundland Power's set-up, as you call it, and the regulatory construct, and given, you know, the execution part of it, and that's common to any utility, and given Newfoundland Power's ability to earn the return since 1996 each and every single year, what could cause Newfoundland Power to fail to earn its allowed ROE in the future, given that it's essentially always earned it in the past?

MS. PERRY:

A. Mr. Chairman, Newfoundland Power is very much like a normal business in so many ways and we, from a financial risk perspective, we still take the risk of forecast risk between test years. We take the risk with respect to management of our power supply costs as it relates to demand cost, operating the system. We can tell from Friday that we incur cost, certainly unexpected cost that are not necessarily within Newfoundland Power's control or budget. We have an 80 million dollar capital plan that we manage daily to ensure that it comes in on time, on budget, because if not, we have to finance that capital program. We have to depreciate that

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capital program. And I'll bring the Board back to 2010 when Igor actually happened and yes, we earned our return in that year, we did, but Igor was a big significant event. It was a little bit of -- I'm not sure I should say this, but good luck on our side in the fact that sales were higher than what we expected. But other than that, Newfoundland Power would have, in that particular year, certainly been at the lower end of its range of return.

MR. JOHNSON:

Q. Still in all, it would have been a reasonable return, because anything in the range is reasonable.

MS. PERRY:

A. Well, it would have been below the allowed.

MR. JOHNSON:

Q. Pardon me?

MS. PERRY:

A. It would have been below the allowed return.

MR. JOHNSON:

Q. If that had transpired. In terms of -- I'd like to bring you to a question that Newfoundland Power asked to Dr. Booth in

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Newfoundland Power CA-03. The question is: with reference to CA-NP-004(A), Dr. Booth states "I would accept that Newfoundland Power's average business risk and assessment that Newfoundland Power seems to accept and also that it has lower financial risk which Newfoundland Power also seems to accept." And the question that was sent back to Dr. Booth was "please indicate specifically where in the response to Request for Information CA-NP-04 Newfoundland Power indicates that it has lower than average financial risk." And Dr. Booth's reply is "Newfoundland Power's target common equity ratio of 45 percent is higher than that typically approved for Canadian regulated -- for regulated Canadian electric utilities. With a higher common equity ratio, by definition, there is lower financial risk to the common equity holder." And is that, is Dr. Booth's answer disputed by Newfoundland Power?

MS. PERRY:

A. I don't think it's disputed. I think what we're saying is that all else being equal, with a higher common equity ratio, that lowers the financial risk, just the financial risk, of a utility.

MR. JOHNSON:

Q. So that's all he was saying, and we thought it odd that Newfoundland Power would -- in any event, we're not in disagreement that the higher common equity ratio lowers Newfoundland Power's financial risk?

MS. PERRY:

A. I don't believe so, Mr. Johnson.

MR. JOHNSON:

Q. Okay. And does Newfoundland Power accept that there's a difference between financial risk and business risk?

MS. PERRY:

A. Yes, we do.

MR. JOHNSON:

Q. Okay. And how does Newfoundland Power assess its business risk?

MS. PERRY:

A. Well, there's -

MR. JOHNSON:

Q. Do you have average business risk?

MS. PERRY:

A. Our experts have determined that we are an

average business risk. The Board, at the last hearing, cited that Newfoundland Power was considered to be an average risk utility. The way -- back to the question on how we assess business risk, we look at the different areas of business risk which certainly include, as Mr. Ludlow talked about: our demographics; our population which was forecast to decline lower than any other province or I should say decline in comparison to all other provinces; the size of Newfoundland Power relative to other utilities; look at our operating conditions; our source of power, single source of power. We look at our cost flexibility. And we've displayed all of this in our evidence in this proceeding and we've made the observation that we do not believe that our business risk have changed materially since the last rate filing, and at that time, the Board concluded at that time that Newfoundland Power was an average risk utility.

MR. JOHNSON:

Q. What I'm getting at and what I'm asking is in relation to Newfoundland -- you've indicated there's a difference between business risk and

financial risk, but what I'm asking you is does Newfoundland Power consider that it has average business risk of a regulated utility in Canada?

MS. PERRY:

A. No, I don't believe we do. I think that we consider we -- we've considered the fact that given the fact that we are small and low growth, which is what the Board has cited, as being important in the determination of our overall risk and the 45 percent equity ratio, which lowers our financial risk, offsets that heightened level of business risk so that overall we're average.

MR. JOHNSON:

Q. So your business risks are above average?

MS. PERRY:

A. It's probably not for me to observe because it's relative to what, right. I mean, what is it relative to? What I'm saying is that we've displayed our business risk and we've said they've not materially changed since the last proceeding and at that time, the Board indicated that overall we were an average risk utility, and I would agree with that

observation.

MR. JOHNSON:

Q. Yes, and you've stated that, but does Newfoundland Power consider that its business risk are greater than average of the Canadian utilities?

MS. PERRY:

A. Mr. Chairman, I want to say yes. I'm not sure I'm qualified to do so, so -- but I do so on the basis of the fact that when I look at our population, we are forecast to decline. No other province is forecast to decline. Our demographics are on the bottom. Our forecast GDP outlook is lower than the rest of Canada. And I can't help but think that those prevalent pieces of information matters to the assessment of Newfoundland Power's business risk. I'm not the expert. I would look to the experts for that, but I think that the size of Newfoundland Power, the low growth and the other things that I've mentioned certainly weigh into my belief that Newfoundland Power has certain business risks not faced by others, yes.

MR. JOHNSON:

Q. But you don't face avalanches.
MS. PERRY:
A. Not yet.
MR. JOHNSON:
Q. But in terms of you reference the negatives for Newfoundland Power, but you don't talk about any of the positives. What are the positives, Ms. Perry, for Newfoundland Power?
MS. PERRY:
A. I'm not sure I understand the question, Mr. Johnson.
MR. JOHNSON:
Q. Well, concentration in the market. I mean, DBRS, one of your bond rating agencies, indicates, do they not, that you have market dominance on the island?
MS. PERRY:
A. Yes, and they also mention that we have limited growth.
MR. JOHNSON:
Q. But limited growth as well, growth -- high rates of growth involves risk as well, does it not?
MS. PERRY:
A. I believe so. You have to fund and finance

that rate base growth.
MR. JOHNSON:
Q. And then there's forecasting risk that might be elevated through that?
MS. PERRY:
A. Certainly.
MR. JOHNSON:
Q. Which Newfoundland Power wouldn't have in a more conservative mature growth environment?
MS. PERRY:
A. That is true, but what Newfoundland Power faces is the fact of urbanization and the fact that we have a number of municipalities that are lowering in their population, but we're still having to service that population. So there's differences with all markets, I believe.
MR. JOHNSON:
Q. And Newfoundland Power, as Ms. McShane talked about the difference in sectors, Newfoundland Power is in the -- you know, actually Newfoundland Power has a fair amount of assets in transmission, do they not, Ms. Perry?
MS. PERRY:
A. We have a certain percentage of assets in

transmission, yes.
MR. JOHNSON:
Q. Yes, and that would be part of the lowest segment of risk in the country, as Ms. McShane indicated?
MS. PERRY:
A. I believe that was her testimony yesterday, yes.
MR. JOHNSON:
Q. And then in terms of distribution aspect, she puts that a bit above transmission but certainly below natural gas on a segment basis, you heard that?
MS. PERRY:
A. Yes, I heard that.
MR. JOHNSON:
Q. Okay. So how do you -- do you discount where you sit in the sectors in terms of how suddenly you then determine that business risk for Newfoundland Power is greater than average?
MS. PERRY:
A. Again, I knew that by saying yes that would be problematic because I'm not the expert and I certainly am not the one to perform that

business risk analysis such that was done by Ms. McShane to compare to distribution, transmission, natural gas. What I'm saying is that is what I know.
MR. JOHNSON:
Q. And let us agree then on this: your assessment on it is not a professional assessment at all. It's more of a -- it's -- well, I won't say professional, but it's not an expert assessment in any way and it's a rather subjective assessment, is it not?
MS. PERRY:
A. I disagree in the fact that we're coming from the last rate case and we've articulated the business risk of Newfoundland Power at a time when the experts filed evidence the last time about Newfoundland Power's business risk. We've laid out the significant business risk that we see. We've stated that we believe they've not materially changed. So I don't see the precipitating factor that would have changed Newfoundland Power's assessment of being an overall average risk utility. The Board cited that our low growth small profile was offset by the 45 percent and we're just

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simply saying that nothing has changed since then, and I guess that's about as far as my professional judgment can take it.

MR. JOHNSON:

Q. Right, but I guess it would be fair to say that on behalf of Newfoundland Power, you can state that the Board should consider relative rankings of the utilities in terms of transmission, distribution, gas, vertically integrated? Would that be fair?

(10:15 a.m.)

MS. PERRY:

A. I think, Mr. Chairman, I'll let the Board decide what they consider as evidence.

MR. JOHNSON:

Q. Do you consider it as relevant?

MS. PERRY:

A. All information is relevant, Mr. Johnson.

MR. JOHNSON:

Q. Including your market dominance and all those other factors?

MS. PERRY:

A. Yes, I would agree.

MR. JOHNSON:

Q. Yes, okay. But I take it, if you would not --

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I take it you would not disagree that if the Board were to conclude that Newfoundland Power has average business risk relative to other utilities and lower than average financial risk as you've conceded that it would be obvious that Newfoundland Power's overall risk would be lower than an average risk, an average business risk utility?

MS. PERRY:

A. I believe that risk is the total of all three, which is business, financial and regulatory and if the Board were to decide that Newfoundland Power had lower business risk than what it had the last time it was here -

MR. JOHNSON:

Q. No, if Newfoundland Power had average business risk and accepted what you've indicated that the financial risk is lower, would it not be obvious that Newfoundland Power's overall risk would be lower in that scenario?

MS. PERRY:

A. I think by the summation, yes, that's true, but Mr. Johnson and Mr. Chairman, I would note that I'm not aware of what has changed since the 2009 hearing with respect to Newfoundland

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Power's business profile.

MR. JOHNSON:

Q. Well, we certainly have some evidence to compare its profile to from BC. In any event, we will go to another topic for a bit, and I'll ask you to go to page 311. You're showing in Table 3.8 finance charges for the company. You're showing your average debt, finance charges and average cost of debt over 2010 to 2014 and Ms. Perry, the average -- as I've noted, the average embedded debt cost is shown and we note that it was 7.46 percent as an average cost in 2010 and has declined slowly since then and is forecast at 7. 05 percent in 2013 and 6.9 percent -- 6. 96 percent in 2014, and is this relatively slow decline in the average cost of debt, is this because Newfoundland Power is relatively slow growing with little new debt and that therefore the embedded debt costs will mainly decline due to refinancing of existing debt?

MS. PERRY:

A. In part, I would agree. I mean, your cost of debt will change as you term out and pay off existing debt and refinance your debt, yes.

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And it matters with respect to your proportion of your long term with your short term at any point in time.

MR. JOHNSON:

Q. Right. So if Newfoundland Power was growing rapidly and having to go to the markets, we would expect to see average cost of debt come down more rapidly than what we're seeing in this case?

MS. PERRY:

A. At today's current rate, yes.

MR. JOHNSON:

Q. And could I direct your attention to Dr. Booth's testimony at page 28?

MS. PERRY:

A. Thank you.

MR. JOHNSON:

Q. Ms. Perry, Dr. Booth has prepared a graph which tracks both Scotia Capital's long term A bond yields and the Bloomberg derived utility long term yield and you see that before you?

MS. PERRY:

A. Is that on page 28, Mr. Johnson?

MR. JOHNSON:

Q. Yes, ma'am.

MS. PERRY:
A. Okay, yes.
MR. JOHNSON:
Q. And Dr. Booth tells me that the average for the Scotia Capital long term bond yields was 5.42 percent in 2010 and 4.92 percent in 2011 and 4.2 percent in 2013 and he tells me that the utility, derive utility long term yield would be about 20 basis points lower. Does this sound about right to you?
MS. PERRY:
A. I'll accept that that's what this is saying.
MR. JOHNSON:
Q. Okay. And so if we keep those figures in mind and look at Newfoundland Power's embedded debt costs of 7.46, 7.31, going down to 7.05 to 6.96, it would be true that rate payers through Newfoundland Power's revenue requirement are paying about two percent more each year than Newfoundland Power's market debt cost? Would that be right?
MS. PERRY:
A. Newfoundland Power is paying its current cost of debt, its embedded cost of debt.
MR. JOHNSON:

Q. I understand.
MS. PERRY:
A. Because you don't pay your market cost of debt.
MR. JOHNSON:
Q. I understand, but relative to what's out there on the market, the embedded cost is about two percentage points more, right?
MS. PERRY:
A. That sounds reasonable.
MR. JOHNSON:
Q. Okay. And would -- and I guess this goes back to the earlier point as to whether you would believe that Newfoundland Power should get a higher ROE because it has a higher embedded debt cost?
MS. PERRY:
A. Mr. Chairman, I think there is some correlation between your cost of debt and your cost of equity. The reality is our average cost of debt is, on average, seven percent. So I think there is some correlation between your cost of debt and your cost of equity, yes.
MR. JOHNSON:

Q. And do you think that Newfoundland Power should have higher common equity ratio because it has higher embedded debt costs?
MS. PERRY:
A. Well, I know that with a lower common equity ratio, your financial risk is increased, so with a higher embedded cost of debt, you'll have higher fixed charges, so that, in my mind, increases the financial risk exposure to Newfoundland Power. So I believe so, yes.
MR. JOHNSON:
Q. Could I ask you to turn up the Fortis MD&A?
MS. GLYNN:
Q. That's Information Item No. 6.
MS. PERRY:
A. Oh, this is the information. I got it right here.
MR. JOHNSON:
Q. Ms. Perry, in particular, if I could ask you to turn to page 37, and the capital structure is shown in the box there, and I take it that you'll agree that that indicates that Fortis itself has 57.1 percent debt, 8.3 percent preference shares and 34.6 percent common shares?

MS. PERRY:
A. Yes, I can confirm that.
MR. JOHNSON:
Q. And would you accept that Fortis has a consolidated common equity ratio of 35 percent?
MS. PERRY:
A. Yes, that's what it's showing here.
MR. JOHNSON:
Q. Okay, yeah. And in terms of the financial arrangements between its operating subsidiaries and the parent company, as you go down to the bottom of page 37, first of all it sets out the credit ratings of Fortis, which is Standard and Poors A minus and DBRS A low as their unsecured debt credit rating, and it says "the above noted credit ratings reflect the corporation's low business risk profile and diversity of its operations, the stand alone nature and financial separation of each of the regulated subsidiaries of Fortis, management's commitment to maintaining low levels of debt at the holding company level, the corporation's reasonable credit metrics and its demonstrated ability and continued

focus on acquiring and integrating stable regulated utility businesses financed on a conservative basis."

And I take it your -- if we look at the common share -- if we flip back and look at, on page 22, which sets out the allowed common equities of each of Fortis' companies, obviously everybody is at 40, with the exception of Fortis Alberta who's at 41, Newfoundland Power is at 45, and in terms of the Fortis family of companies, would Newfoundland Power be an average business risk within Fortis, the Fortis utilities?

MS. PERRY:

A. I've not made that assessment, Mr. Johnson.

MR. JOHNSON:

Q. So you don't know?

MS. PERRY:

A. That's correct.

MR. JOHNSON:

Q. If we add up all of the equity in the Fortis companies that are shown there, as we've noted each utility has at least 40 percent common equity, whereas as we've demonstrated, the consolidated common equity ratio of Fortis

itself is only 35 percent. What does this tell us, Ms. Perry?

MS. PERRY:

A. I'm not sure I understand the question, Mr. Johnson.

MR. JOHNSON:

Q. Doesn't it mean that Fortis is financing its equity investment in its subsidiaries with other securities other than straight common equity?

MS. PERRY:

A. Yes, that's what it's showing here, yes.

MR. JOHNSON:

Q. And as we've seen, Fortis has 8.3 percent preference shares itself, correct?

MS. PERRY:

A. Yes. I'm not sure what type of preference shares, but yes.

MR. JOHNSON:

Q. And I take it there's no question that if we replaced five percent of Newfoundland Power's common shares with preference shares that Newfoundland Power's capital structure would be in line with the other Fortis utilities and indeed with Fortis itself?

MS. PERRY:

A. Mathematically, yes, but there's a lot of complications with just swapping out five percent common equity with five percent preferred shares and I've displayed those in my opening.

MR. JOHNSON:

Q. And we'll talk about those. And in terms of the mechanisms of preferred share issuance, if Newfoundland Power were to issue preference shares, that would be done with the assistance of Fortis no doubt?

MS. PERRY:

A. Can you repeat the question, Mr. Johnson?

MR. JOHNSON:

Q. If preference shares were to be issued in Newfoundland Power, how would that -- how would you go about that?

MS. PERRY:

A. Well, if it was deemed appropriate to issue preference shares, Newfoundland Power would issue preference shares. We operate Newfoundland Power on a stand-alone basis and that pertains to the financing of Newfoundland Power as well. And I believe it was in 2003-

2004 where the Board, at that time -- and there was concern around that time with respect to certain credit rating linkages between Fortis and Newfoundland Power and the Board clearly stated at that time that it felt it was in the best interest of customers and Newfoundland Power to operate as a stand-alone utility. So if we were to issue and deem it appropriate, which would be a battle to begin with, but if we were to deem it appropriate to issue preference shares, we would have to issue them on our own as Newfoundland Power, not with Fortis.

(10:30 a.m.)

MR. JOHNSON:

Q. And you indicated in your direct testimony that that would be troublesome, and why would that be, in terms of actually issuing preference shares to investors?

MS. PERRY:

A. Mr. Chairman, as I said, we're relatively a small player in the market, so we're an unknown player with the market. Most of our long term debt deals are actually privately placed. So I've had discussions with banks around issuing a 40 million dollar preference share issuance and the response was that would be unusual because that's a very small issuance. Usually you see the preferred share market to be much larger than that. And as I said, where we are an unknown name to that market, to the preference share market, we would certainly have to go through a pretty significant investment profile prior to issuing and I have asked about pricing with respect to preference share, because we're always interested in getting the lowest price, and it's viewed that it would be no more efficient than if we issued long term bonds. That's the view today. So if we could issue it probably would be at a higher cost than long term debt.

MR. JOHNSON:

Q. When was the last time that was investigated?

MS. PERRY:

A. I would say mid December I confirmed by conversation around preference shares, based on Dr. Booth's evidence.

MR. JOHNSON:

Q. And in terms of there being a market for

preference shares, you're aware that there's a sizable market out there for people who desire preference shares to invest in no doubt?

MS. PERRY:

A. Certainly. There's a preference share market. It's just we are a small issuer, so we're not a known issuer in the market and normally preference share issues are substantial, and I know Fortis just issued one, I believe it was over 200 million.

MR. JOHNSON:

Q. But that was in November of 2012?

MS. PERRY:

A. Yes, I believe around that time.

MR. JOHNSON:

Q. I think the first preference shares had a yield of 4.75 percent.

MS. PERRY:

A. I would have to confirm but that sounds in the ballpark.

MR. JOHNSON:

Q. Would you take that, subject to check?

MS. PERRY:

A. Yes.

MR. JOHNSON:

Q. In terms of capital market conditions, Ms. Perry, I take it that you would agree that capital market conditions are easier now than they were in 2009 when the Board last heard cost of capital testimony?

MS. PERRY:

A. Mr. Chairman, I will agree that they're probably easier than the first part of 2009, but by the time we got to the hearing in 2009, the markets had somewhat rebalanced from where they were at the lowest level and I'm not sure that I see a lot of difference since then. There's been a lot of ups and downs and in betweens since the latter part of 2009 and certainly one of the ways I gauge the capital markets is looking at Newfoundland Power's credit spreads and our credit spreads are roughly the same as what they were at the end of 2009. They haven't changed significantly.

MR. JOHNSON:

Q. In terms of your assessment of the capital markets, do you have any expertise in the capital markets or is this just -- are we on the level of your impression about it, Ms. Perry?

MS. PERRY:

A. No, I would not go as far as to say that I'm an expert in capital markets and certainly we provided evidence with our witnesses on that.

MR. JOHNSON:

Q. Okay. And I just wanted to get that clarified, if that's the case. If I could bring you to page 53 of this Fortis MD&A? It indicates as a subsequent event that in October of 2012, Fortis Alberta issued 40-year 125 million dollar 3.98 percent senior unsecured debentures, the proceeds of which are being used to repay borrowings under the company's credit facility, fund future capital expenditures and for general corporate purposes. Dr. Booth advises me that according to the Wall Street Journal this was at 140 basis point premium to equivalent maturity long Canada bonds. Would you accept that?

MS. PERRY:

A. I accept that, yes.

MR. JOHNSON:

Q. And Fortis Alberta, they're rated A low by DBRS? Would that be correct, Ms. Perry?

MS. PERRY:

A. I would have to confirm that.

MR. JOHNSON:

Q. Okay. Would you accept that they are rated A low by DBRS and BAA1 by Moody's?

MS. PERRY:

A. Subject to check, yes.

MR. JOHNSON:

Q. And A minus by S&P?

MS. PERRY:

A. Again, subject to check.

MR. JOHNSON:

Q. Okay. Do you -- you deal with trying to raise funds through bonds, et cetera. Would you believe that Fortis Alberta could have raised 40-year sub four percent debt in 2009?

MS. PERRY:

A. I would have to go back there and just see what they were issuing at at that time. The coupon rate that we're looking at here is a product of the decline in the bond yields, the Canada bond yields. So it's not all reflective of the bond spread, the utility bond spread.

MR. JOHNSON:

Q. But in terms of the availability to access

debt, that has -- would it be your observation that that has improved, relative to a few years ago, especially at those low, low rates?

MS. PERRY:

A. Mr. Chairman, I'll agree with the low rates and as I said, it's a reflective of the long Canada bond yield, but I'm not sure I would go as far and say that the market is any better since the latter part of 2009. Now we have not issued any debt since 2009, so I have nothing directly to compare it to.

MR. JOHNSON:

Q. At page 40, just a little bit below the chart, it indicates that "in March 2012, Newfoundland Power renegotiated and amended its 100 million dollar unsecured committed revolving credit facility, obtaining an extension to the maturity of the facility from August '15, August 2015 to August 2017. The amended credit facility agreement reflects a decrease in pricing but otherwise contains substantially similar terms and conditions as the previous credit facility agreement" So in terms of the decrease in pricing, can you indicate what that was?

MS. PERRY:

A. So this refinancing was on our 100 million dollar unsecured short term credit facility, and so periodically, if the market is right, we will -- we have a pricing grid within that particular credit facility and if the pricing should contract, then we will take opportunity of that and refinance, and that's what we have done.

MR. JOHNSON:

Q. So what was the decrease in pricing that was experienced?

MS. PERRY:

A. I don't have it in front of me now. I wouldn't -- I'm not sure what the actual decline was, and certainly the savings would depend on the amount of short term borrowings that we would have in any particular time.

MR. JOHNSON:

Q. Right, and they say contains substantially similar terms and conditions as the previous credit facility agreement, and I think there was an adverse conditions clause that had been there before or an adverse material change clause that had been removed.

MS. PERRY:

A. My memory is that the material adverse clause was removed prior to this extension. It was removed some time ago.

MR. JOHNSON:

Q. And the nature of that clause, when it existed, did what? What was its effect?

MS. PERRY:

A. I would have to go back and actually read that clause again because it's been sometime since it's been in Newfoundland Power's credit agreement. I believe that was removed some years ago. I'd have to check, Mr. Johnson.

MR. JOHNSON:

Q. I wonder if Ms. Perry and Mr. Kelly wouldn't mind filing what that clause stated as an undertaking?

KELLY, Q.C.:

Q. That's fine, Mr. Chairman.

MS. PERRY:

A. Sure, yeah.

MR. JOHNSON:

Q. Ms. Perry, moving to another topic. Since the last general rate application, there have been a number of stand-alone applications that

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Newfoundland Power has been able to make to the Board. For instance, by order of P.U. 30 (2010) the Board approved deferred recovery by Newfoundland Power of nearly 2.4 million in 2011 costs, and then P.U.12, I think 20 -- I don't know if it was 2010 or 2011, the Board approved recovery of 2.4 million in 2012 costs, and then we had the Board's order in P.U.17 ('12) which approved deferred recovery by Newfoundland Power of two and a half million in 2012 costs as part of its determining Newfoundland Power's cost of capital, right?

MS. PERRY:

A. Yes, I believe that to be correct.

MR. JOHNSON:

Q. And were there any other one-of applications of that nature over that period that you can think of?

MS. PERRY:

A. Other than to apply for suspension of the formula.

MR. JOHNSON:

Q. Right, okay. And in terms of Newfoundland Power applying for determination of cost of

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equity without necessity of filing a general rate application, are you -- which was done, for instance, in 2012 -- are you aware of how rare an event that is in the United States, for instance? Ms. McShane indicates that she's not aware of an instance where a US utility sought and was granted a determination of its cost of equity without necessity of filing a GRA. Are you aware of that?

MS. PERRY:

A. No, I wouldn't be able to comment on what happens.

MR. JOHNSON:

Q. Can you tell us what advantage or benefit it was, sitting in your chair as CFO to Newfoundland Power, to be able to bring forward such an application before the Board, to the Board for its determination outside of a GRA?

MS. PERRY:

A. Well, Mr. Chairman, the application with respect to cost of capital was certainly precipitated on the formula producing a return that we deemed to be unfair. So in the absence of the formula, Newfoundland Power

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would likely not have applied for 2012, but given that the issue that we had to deal with was our cost of equity, then we sought a cost of capital application to deal with that one sole issue.

MR. JOHNSON:

Q. And do you know whether it has precedent even in other Canadian jurisdictions?

MS. PERRY:

A. I believe cost of capital applications are held in Alberta. I would have to confirm. I'm not sure.

MR. JOHNSON:

Q. On a stand-alone basis like that? And in this proceeding, Ms. Perry, Newfoundland Power has applied to amortize the recovery over a three-year period of a forecast 2013 revenue shortfall of an estimated $980,000 which was agreed to, and tell us why this request was important to the company and why it was sought.

MS. PERRY:

A. With respect to that one amortization, Mr. Johnson?

MR. JOHNSON:

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Q. Yes.

MS. PERRY:

A. Or all of the amortizations?

MR. JOHNSON:

Q. No, no, just that one.

MS. PERRY:

A. Well, the three-year amortization of the shortfall was in line with the proposed amortization period for a number of other regulatory amortizations that we had and in the past, amortizations have ranged, I will say, from three to five years, but certainly three years is certainly reflective of the time period upon which Newfoundland Power would generally file a general rate application.

MR. JOHNSON:

Q. But we're talking -- I guess you've focused on the amortization period, but I'm focusing on the forecast 2013 revenue shortfall. How would that revenue shortfall have come about, the 2013 revenue shortfall of an estimated 980,000?

(10:45 a.m.)

MS. PERRY:

A. So as a product of filing for a double test year, 2013 and 2014, it would be hard to imagine that if we set rates based on 2014, full year test year, and that if we apply that then to the 2013 on March 1st that it would all balance in one fold. So I would suspect it's very common that you would end up not perfectly squared with balancing the records when you are talking different implementation times when you're dealing with a double test year. So that's how the 980 came about.

MR. JOHNSON:

Q. And in terms of the goal of Newfoundland Power to have rates implemented by March 1st, 2013, I take it the company wanted a mechanism in place to ensure that in the events that rates couldn't be implemented in time for March 1st, 2013, that the company was made whole nonetheless, correct?

MS. PERRY:

A. I believe that's a fair observation in that we are dealing with two test years, so we are considering the complete revenue requirement for those two years, yes.

MR. JOHNSON:

Q. And in the last GRA in 2009, that was to set rates for 2010. Newfoundland Power wanted rates to come in force January 1st of 2010, did it not?

MS. PERRY:

A. Yes, that is correct.

MR. JOHNSON:

Q. And my recollection, Ms. Perry, is that to facilitate this, this Board in fact issued an order in advance of providing its reasons for decision, which reasons for decision came out Christmas Eve, if I recall, and so that you didn't have to wait for the full reasons in order to go ahead implementing rates. Do you recall that?

MS. PERRY:

A. Yes, I recall certain of that process, but yes, I believe a decision came out before all of the particulars of the decision, yes.

MR. JOHNSON:

Q. What was the advantage or the benefit to Newfoundland Power of the Board doing that?

MS. PERRY:

A. I don't believe there was any advantage to Newfoundland Power. This was -- we filed a

test year to recover -- have a reasonable opportunity to recover 2010's test year cost and in the event that rates, for reasons of timing, were not to be implemented on January 1, then Newfoundland Power would have actually not have had the opportunity to recover the full revenue requirement that was just considered before the Board.

MR. JOHNSON:

Q. Yeah, so the obvious advantage or benefit to Newfoundland Power by the Board issuing its order in advance of when it was ready to issue its decision was that it provided Newfoundland Power the opportunity to earn the return over the full of 2010 so that you weren't delayed in any revenue, correct?

MS. PERRY:

A. I'm still not seeing the advantage to Newfoundland Power. We're dealing with a full year test year, so we're not recovering any more or any less than a full year test year.

MR. JOHNSON:

Q. Ms. Perry, in that instance, in connection with that instance, one thing I never see in Newfoundland Power's materials in GRAs or

otherwise or in your credit opinions is any complaint about regulatory lag in this jurisdiction. Would you agree with that?

MS. PERRY:

A. I would agree with that, yes.

MR. JOHNSON:

Q. Yeah. And regulatory lag, how would that be of a concern to a utility, if there was significant regulatory lag in the utility's regulatory set-up?

MS. PERRY:

A. I think it has to do with just the financial uncertainty as to the operations of that utility in a particular year. If there was uncertainty with respect to how things are going to operate -- and we are a regulated utility so it matters with respect to the construct as to how we're to operate, so without knowing what it is, it's hard to predict because it comes from decisions of the Board. So it's better to know in advance and prepare for what is coming, as opposed to being behind it.

MR. JOHNSON:

Q. So what sort of problems could arise for a

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regulated utility that would result from regulatory lag, just some concrete examples?

MS. PERRY:

A. Well, I'll go back to the 2012 cost of capital, I guess. That one, from a timing perspective, we were into 2012 before we had a cost of capital determined. So we're already midway through the year. So if we were approved or ordered a rate of return that was I'll say deemed unfair or lower than the rest of the country, then we only have six months to try to deal with it then, because the uncertainty was there, so up until mid 2012, it was unknown as to what it would be. We only have six months now to try to do things to get us to the top of a return.

MR. JOHNSON:

Q. Can you provide any other further illustrations of where regulatory lag, if it existed for Newfoundland Power, would cause a company difficulty?

MS. PERRY:

A. I guess in terms of cost recovery, if we were -- if we put a proposal to this Board to defer some regulatory amortizations, you know, as

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we've done in 2011 and '12, and if there was an order that disallowed something that we thought were to be allowed, then that puts the utility in a hard situation with respect to looking at its financial condition for that particular year. I mean, you just lose time to recover from the decisions of the Board.

MR. JOHNSON:

Q. It's five to 11. Were you planning, Mr. Chairman, to break at 11, was it?

CHAIRMAN:

Q. Yes.

MR. JOHNSON:

Q. If you -

CHAIRMAN:

Q. Is this a good hiatus for you now?

MR. JOHNSON:

Q. I think so.

CHAIRMAN:

Q. Okay then, we shall reconvene at 25 after.

(BREAK - 10:53 a.m.)

(RESUME - 11:29 a.m.)

CHAIRMAN:

Q. Okay, we're still with you, Mr. Johnson.

MR. JOHNSON:

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Q. Thank you. Ms. Perry, as you alluded to before the break, Newfoundland Power has set up its general rate application to use two test years. What was the rationale?

MS. PERRY:

A. I believe, Mr. Chairman, that the rationale was based on timing. Historically when we filed general rate applications we try to file closer to the beginning of the year, so that we're given a reasonable opportunity to hear the proceeding and implement rates for January 1st of the upcoming year. But starting in September, we viewed that it would be a stretch to assume that we could get rates for January 1, so with that in mind, we filed a double test year, which from records at Newfoundland Power, I believe the last one we filed was 2003, 2004.

MR. JOHNSON:

Q. The double test year, I mean, we're still only very early in 2013 and you have a mechanism to cover yourselves off from the interim rates or whatever for 2013. I'm not understanding fully the rationale for 2014 also being a test year.

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MS. PERRY:

A. Well I guess to clarify, another part of the decision was simply around by the time this proceeding ended, I guess depending on the outcome of the order, we could have been in a position where we would have had to file again for '14, you know, so I think it's forward visibility. You're partway into 2013, it's not unreasonable and certainly we have done this in this jurisdiction before, to look forward further than just seven months, so that's what we had done.

MR. JOHNSON:

Q. Talk to me about the forward visibility part. The forward visibility of looking forward to 2014, what's the advantage of Newfoundland Power making 2014 a test year from the point of view of forward visibility?

MS. PERRY:

A. I'm not sure it's an advantage again, Mr. John's, the only difference is that you lay out your forecast revenues for two years and rates are structured such that you're given a reasonable opportunity, an opportunity to earn your return in each of those years and so part of the decision, based on regulatory efficiency, I don't really see the advantage of Newfoundland Power with that.

MR. JOHNSON:

Q. Ms. Perry, you seem not to want to concede much in the way of advantages to Newfoundland Power this morning. I think it permeates a lot of what you had to say here and I've had to really go digging a bit more than I thought I had to. A moment ago you said that it allows you to forecast revenues in 2014, that's one of the things you said about a 2014 test year, correct?

MS. PERRY:

A. To lay out a test year, you have to forecast your revenue requirement, yes.

MR. JOHNSON:

Q. Yes, and you said "revenues", not "revenue requirement". Part of what you're forecasting as well in capturing in the 2014 test year is your estimated costs for 2014, correct?

MS. PERRY:

A. Certainly, it's -

MR. JOHNSON:

Q. And you're getting a chance to have rates to

reflect those costs in 2014 without having to come back or without the uncertainty of living with costs based on a 2013 test year, correct?

MS. PERRY:

A. I see the double test years as slightly different than that. You're laying out annual revenue requirements for Newfoundland Power with your forecast cost, as you would in a single test year, and based on Board orders and implementation of customer rates, then that will just provide Newfoundland Power an opportunity to recover the forecast costs that we've laid before this Board.

MR. JOHNSON:

Q. Okay, but let's get basic here. In a normal case if you choose one test year, say 2013 test year, you said that's going to be our test year and if we can't get rates by before March 1st, we might have to do something on an interim basis or something like that. And in that instance, in that case, Ms. Perry, what would happen in 2014 if 2014 was not a test year?

MS. PERRY:

A. So if we were going to go with a single test

year, we would have to look at the full revenue requirement for 2013 and we would have to prepare the forecast on a different basis than we've done here today, and just by way of example, we've assumed in our forecast that the energy supply cost variance reserve is going to work for January and February of 2013, so if 2013 were going to be a full test year, a single test year, then we would have to rebase 2013 as if non of the mechanisms were in to play. So it's just a different way of doing much the same thing, I believe.

MR. JOHNSON:

Q. Well, I disagree with you because if we were looking at 2013 as a test year, what would happen in 2014 is that you would have to live with the rates in 2014 based upon what the forecasted revenues and expenses and costs were for the 2013 test year, correct?

MS. PERRY:

A. That is correct, yes.

MR. JOHNSON:

Q. And if 2014 saw a cost escalation for labour or materials or advertisements or any of those things, or pay, that would not be reflected in

your rates per se for 2014, you'd be using 2013 costs, correct?

MS. PERRY:

A. Yes. Mr. Chairman, I would state though that in a single test year, so in preparation of a single test year, we do look forward, so if 2013's proposals was structuring Newfoundland Power to be in a revenue shortfall position in 2014, then I would suggest that probably wouldn't be very good planning on our part because you should plan a rate case to be sufficient to allow a utility to go several years before rebasing costs. It is not our intent to come in here every single year, so when we even file single test years, we would look forward to ensure that the proposals we're putting forward, like the amortization periods, recovery periods, are all in line with trying to keep us out of here basically for a number of years. So I think the concepts still apply to a single verses a double test year.

MR. JOHNSON:

Q. But surely outside of something big coming on a horizon, there's a benefit of having 2014 set up as a test year because you get to forecast those 2014 cost--expenses, and have them actually reflected in rates for 2014 which is an advantage over a situation of a single test year where the 2014 costs would happen and they would be just dealt with in a normal event. I thought that this was an obvious point, it wouldn't be a major point of contention, Ms. Perry.

MS. PERRY:

A. I will agree, Mr. Johnson, that we are forecasting 2014's costs. I guess why I'm a bit reluctant, Mr. Chairman, to say that there's an advantage is that it's just still a forecast. So at any point in time we're still dealing with forecast numbers, so -

MR. JOHNSON:

Q. As the CFO of Newfoundland Power, there's going to be increases in certain operating costs in 2014 over 2013, I take it.

MS. PERRY:

A. Yes, that is correct.

MR. JOHNSON:

Q. Yes. And do you know anything about historical test years and how they operate?

MS. PERRY:

A. In any particular jurisdiction, Mr. Johnson or -

MR. JOHNSON:

Q. No, just the concept of in this jurisdiction we use a forward looking test year and in some jurisdictions they do not, they use a historical test year or part historical, part partial, do you know anything about those historical type test years?

MS. PERRY:

A. From what perspective? Like I understand how they work in terms of they take their historical financials and adjust for known and measurable differences I believe is the -

MR. JOHNSON:

Q. In some instances and some are purely historic.

MS. PERRY:

A. Oh okay.

MR. JOHNSON:

Q. And so, how--what would be the disadvantage of using historical test year to a utility, Ms. Perry?

MS. PERRY:

A. I would suspect historical test years may be problematic if you were in a time of growth or in a time of change because your future is probably not going to look like your past, which is pretty simple, I guess, so in a period of high growth it might be a bit problematic.

MR. JOHNSON:

Q. But in terms of giving visibility, you much prefer as a CFO to be dealing with a future test year as opposed to a past, even a partial past, correct?

MS. PERRY:

A. Our forecast today, yes, they're forward based on the future expectation, but it's built off of the past experience, I guess, of Newfoundland Power. I look at our sales, it comes from our historical sales base, even our operating costs are built off of the previous year, so I get the point that if it's solely based on historical without any adjustment for known and measurable differences, there's some disconnect in the two.

MR. JOHNSON:

Q. You mentioned known and measurable differences

and where did you learn about that concept, through Ms. McShane's evidence?

MS. PERRY:

A. Through a discussion with Ms. McShane and Mr. Alteen, actually.

MR. JOHNSON:

Q. Okay, and so you're aware that--it's regarded, is it not, that forward test years are more advantageous to a utility than historic test years?

MS. PERRY:

A. I wouldn't be able to make that observation, Mr. Johnson.

MR. JOHNSON:

Q. I gave you a cross-examination document in advance and I didn't labour it, but I just want to bring it to you, it's forward test years for US electric utilities prepared for the Edison Electric Institute.

MS. PERRY:

A. Yes, I have that.

MR. JOHNSON:

Q. Dated August 2010.

MS. GLYNN:

Q. Mr. Johnson, we'll enter that onto the record as Information Item No. 11.

MR. JOHNSON:

Q. Thank you.

MS. GLYNN:

Q. It was filed on January 9th.

MR. JOHNSON:

Q. I'm referring to the top paragraph of the executive summary. It indicates, the very first paragraph in the executive summary on this paper is "US investor owned electric utilities, electric IOUs in jurisdictions with historical test year rate cases are grappling today with financial stresses that threaten their ability to serve the public well. Unit costs are rising because growth and sales volumes and other billing determinants is not keeping pace with growth and cost. Cost growth is stimulated by the need to rebuild and expand legacy infrastructure and to meet environmental and other public policy goals. In this situation, historical test years still use in almost 20 United States US jurisdictions can erode credit quality and condemn IOUs to chronic under earning." And then the report goes on, I filed it for the

information of the Board. So there's to be no doubt in your mind, Ms. Perry, that the type of test year that a utility can avail itself of would be a relevant consideration for comparing utilities for cost of capital purposes, correct?

(11:45 a.m.)

MS. PERRY:

A. I will agree that that's what this is saying in this report, yes.

MR. JOHNSON:

Q. And would you depart from what that Edison paper is stating? Because otherwise all you're doing is agreeing that it's in the report.

MS. PERRY:

A. Well I take it that, you know, this is a reputable company doing this report, so I can read what they're saying, but for me to make the assessment myself with my own personal opinion, I mean, I can't provide that.

MR. JOHNSON:

Q. Let us put it this way, Ms. Perry, as CFO of Newfoundland Power, an electric utility that has to keep pace with growth and costs and

rebuilding and expanding legacy infrastructure, all that would apply, would you prefer--would it give you greater visibility to be having the use of a future test year or a historic or a hybrid, what would you prefer?

MS. PERRY:

A. I haven't really thought about it or applied it to Newfoundland Power, but I do see Newfoundland Power's as being a bit of hybrid with respect to how we prepare, given that we do base a lot of our forward costs on past results.

MR. JOHNSON:

Q. But if that be the case, sure there can't be a future test year for anybody because I would have thought that a utility would always consider its past cost history in putting forward a future test year.

MS. PERRY:

A. Maybe Mr. Johnson, yes.

MR. JOHNSON:

Q. And that cannot be unique to Newfoundland Power, surely. So you're not prepared or are you prepared to concede that it's more

advantageous for Newfoundland Power to have a future than a historic?

MS. PERRY:

A. Not at this point I can't, no, Mr. Johnson, no.

MR. JOHNSON:

Q. We touched on the concept of interim rates that are provided for under Section 75 of the Public Utilities Act in this province and in the course, in this very GRA process you would be aware that Newfoundland Power was concerned with whether the Board would be in a position to make necessary determinations on the 2013, 2014 application in a timeframe that would allow Newfoundland Power to implement the change in rates, and so therefore, although the application has now been withdrawn because it got worked out otherwise, but Newfoundland Power applied for interim rates and they stated that if Newfoundland Power was unable to implement the change in the current customer rates in a timely manner, it might be deprived of the opportunity to earn a just and reasonable return on rate base for 2013, as required under Section 80 of the Act. So you

are aware of that application?
MS. PERRY:
A. Oh yes, I'm aware.
MR. JOHNSON:
Q. And you would have recommended that application, no doubt.
MS. PERRY:
A. Yes.
MR. JOHNSON:
Q. Okay, and in terms of the ability of Newfoundland Power to apply for interim rates to the Board, how was that a beneficial feature for Newfoundland Power and its investors?
MS. PERRY:
A. Can you repeat the question, Mr. Johnson?
MR. JOHNSON:
Q. The ability of Newfoundland Power to avail of Section 75 of the Public Utilities Act to apply for interim rates, how was that a beneficial feature for Newfoundland Power and its investors?
MS. PERRY:
A. I think the use of interim rates is a mechanism that is used when rates are not set

at the beginning of a test period. In our case right here, we were going into 2013 without final rates, so it was viewed that an appropriate way to deal with that was to declare the rates interim on January 1st.
MR. JOHNSON:
Q. Would you have concerns if there were legislative barriers to Newfoundland Power's ability to apply for interim rates?
MS. PERRY:
A. At a high level I think I would be concerned, if I was going into a year without certainty around final rates, so I'm not quite sure I understand the question.
MR. JOHNSON:
Q. Well, I'll put it to you and it's not an issue I'll get in deeply with you, Ms. Perry, but I will be bringing it up with some other witnesses here in this case, but in some United States cases, it's certainly with regulatory lag concerns which I will also address, that in some states utilities are allowed to petition for interim rate relief, but in others, they are only permitted to look for such rate relief in emergency situations

and I've read limiting its use to unusually dyer circumstances. And I'd like just to know, obviously it seems to me, as a CFO, that it would be much better to have accessed interim rates than to be put to a jurisdiction where there was impediments in the way of getting interim rates, would you not agree?
MS. PERRY:
A. I don't fully understand the fullness of those jurisdictions, so, but in isolation I do agree with interim rates to be filed, yes, I do.
MR. JOHNSON:
Q. And that's like agreeing that the lights are on. But I mean, what I'm asking, would you agree that there is--that the ability to seek interim rates in an unimpeded fashion is a benefit, an advantage to Newfoundland Power over a situation where there were impediments to it seeking interim relief.
MS. PERRY:
A. Mr. Chairman, I would agree that interim rates is, as I said I agree with in that it allows Newfoundland Power the opportunity to earn a reasonable return in a specific year. Without that or if there were impediments of some sort

that prevented Newfoundland Power a reasonable opportunity to earn its return, yes, I would agree that would be a worse situation than not having an opportunity to earn your return.
MR. JOHNSON:
Q. Newfoundland Power by law in this jurisdiction must seek prior approval for capital budget expenditures, you're aware of that?
MS. PERRY:
A. Yes, I am aware.
MR. JOHNSON:
Q. And the prior approval of capital budgets is something that's referenced, you'll agree with me by the bond rating agencies in Newfoundland Power's case?
MS. PERRY:
A. Yes, I would agree.
MR. JOHNSON:
Q. And why is the prior approval scheme seen to be of benefit to Newfoundland Power?
MS. PERRY:
A. Well I think any time you're spending money, having permission to do so is rule number one, so the point of it is that we only invest in assets that have been reviewed and approved by

this Board as opposed to being so far down the construction of an asset and determining that it was disallowed. So obviously it's better to get permission to spend money prior to spending.

MR. JOHNSON:

Q. And would you consider that whether a utility is subject to a prior approval process that that is a factor that the Board should consider in comparing risks between utilities?

MS. PERRY:

A. It can certainly be a factor, but I think it's in context of how it's been working as well, I suspect. If a jurisdiction is set up such that approval is not sought prior but after and there have been on issues with respect to recovery of prudent costs, then I think that levels the playing field somewhat.

MR. JOHNSON:

Q. But it's not as safe as a prior approval scheme for the utility, is it?

MS. PERRY:

A. I would agree, I think it's worthy to have prior approval before, yes.

KELLY, Q.C.:

Q. Mr. Chairman, many of these questions are hugely hypothetical in terms of, if my friend really wants to get into this kind of a discussion, it really should be with the expert testimony witnesses and be able to put to them the precise parameters of some other jurisdiction, if that's the case. This witness has said, you know, she doesn't have expertise in other American jurisdictions.

MR. JOHNSON:

Q. Mr. Chairman, I have not embarked on bringing Ms. Perry through the American examples in the record, but I think it is certainly material to ask this witness of her view of some of these regulatory features that exist in this jurisdiction because they are, for instance, referred to in the company's own evidence in their exhibits that are attached to their application from Moody's and DBRS and I think it's good to get an on the ground assessment from the witness as to what the benefits are to the utility of these, so I'm just going down through them one at a time, I'm not bringing her through, you know, Vectren or Consolidated and I don't understand why Mr.

Kelly should interrupt me.

CHAIRMAN:

Q. Carry on.

MR. JOHNSON:

Q. Regarding litigation, Ms. Perry, would it be fair to say that Newfoundland Power is not involved in much litigation?

MS. PERRY:

A. I would say that's a fair observation, yes.

MR. JOHNSON:

Q. So that would obviously not be something that you and your team would have to devote much time and attention to?

MS. PERRY:

A. That's correct.

MR. JOHNSON:

Q. You are aware with the concept of accelerated depreciation for tax purposes?

MS. PERRY:

A. You would have to explain that one a little bit to me, Mr. Johnson.

MR. JOHNSON:

Q. Well I understand that from time to time governments, to stimulate the economy, will permit companies to write down assets quicker

in an effort to stimulate the economy, you know, sort of a stimulus type mechanism, and that would have benefits to utilities, I take it, and their investors, would it not? If you were allowed to write down an asset for tax purposes more quickly?

MS. PERRY:

A. If we were allowed to write down the assets more quickly for tax purposes, that would tend to lower Newfoundland Power's effective tax rate, I would agree, yes.

MR. JOHNSON:

Q. And in terms of this Board's determining whether, because as Newfoundland Power has indicated in response to the Board's staff questions, Newfoundland Power has said that amongst other things an essential characteristic of a fair return is that it is commensurate with that available on investments in comparable risk enterprises. And would you, in the utility context, agree with me that some of the factors to be considered would be competition, whether it's competition that's faced by the utility?

MS. PERRY:

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A. Yes.
MR. JOHNSON:
Q. What sector the particular utility would fall into, whether it be transmission, distribution, vertically integrated.
MS. PERRY:
A. Well I think it would be a consideration, yes.
MR. JOHNSON:
Q. Level of non-regulated business?
MS. PERRY:
A. Yes, I would agree.
MR. JOHNSON:
Q. Test year type?
MS. PERRY:
A. That one I'm not sure about, but -
MR. JOHNSON:
Q. Type and number of customers?
MS. PERRY:
A. I think customer profile could be a consideration, yes.
MR. JOHNSON:
Q. So for instance in Newfoundland Power's case, it's largely residential, commercial and not exposed to industrial, that would be spoken about as a positive in Newfoundland Power's

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risk profile. Do you share that assessment?
MS. PERRY:
A. Was it said by someone, Mr. Johnson, or -
MR. JOHNSON:
Q. Well it's said by your rating agencies.
MS. PERRY:
A. Yes, it was said by the rating agencies, yes.
MR. JOHNSON:
Q. And you would agree with their assessment that that's a risk positive for Newfoundland Power?
MS. PERRY:
A. From a credit rating agency, yes, they look at it as more stable revenue.
MR. JOHNSON:
Q. And from a business perspective it's more stable too, is it not?
MS. PERRY:
A. Yes, but it does have a limited growth side to it as well, I guess, so there's two sides to the coin.
MR. JOHNSON:
Q. Yes, okay. And regulatory supportiveness would be the factor. Now, Ms. Perry, I must say to you that I was a bit surprised to hear that Newfoundland Power considered regulatory

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environment to be generally supportive and I mean, we've heard evidence from an American witness in the last GRA, Mr. Cicchetti who characterized it, and you will recall Mr. Cicchetti testified, he recalled it as exceptional regulation, and he--and as well the bond rating agencies, for instance Moody's talks about how Canada is a very good regulatory environment, always considered this Board to be supportive, and I'm wondering why would it be just considered generally supportive?
MS. PERRY:
A. Well again, Mr. Chairman, I'd hate to try to interpret Mr. Ludlow's words and--but it wasn't meant that it was negative, it certainly, from Mr. Ludlow's perspective, was in relation to other jurisdictions that he's been in and on a relative basis it was comparable to the regulatory support in other jurisdictions, so I didn't see it as a negative, but I think we all agree that we have a supportive regulatory environment.
MR. JOHNSON:
Q. Okay. Regarding weather normalization, Ms.

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Perry, Newfoundland Power has full weather normalization protection and Ms. Perry if Newfoundland Power lost weather normalization protection, like it's had for many years and I'm not advocating that, but Newfoundland Power's risk profile, what would happen to it in that instance?
MS. PERRY:
A. Well certainly the weather normalization smooths, for a lack of a better word, Newfoundland Power's revenue and cost of power for the impact of weather and the variations that are applied to this account would, in essence, hit or be positive to the corporation earnings in those particular years without the weather normalization account, so certainly earnings would be more volatile without it, but as we've said in evidence, the weather normalization reserves are quite common in Canada and so certainly Newfoundland Power is not out of step with having a weather normalization reserve.
MR. JOHNSON:
Q. No, and I'm not suggesting you are, but if you lost the weather normalization reserve, it

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would increase, would it not, your risk profile, do you think?
MS. PERRY:
A. Relative to other utilities with a substantial heating load? Yes, I would agree.
MR. JOHNSON:
Q. Yes, okay. And would you agree with me that weather normalization reserve has played a significant role over the years in reducing earnings volatility of Newfoundland Power?
MS. PERRY:
A. Can you repeat the question, Mr. Johnson?
MR. JOHNSON:
Q. Would it be fair to say that the weather normalization reserve has played a significant role over the years in reducing the earnings volatility of Newfoundland Power?
MS. PERRY:
A. In isolation I would agree, yes, but relative to other utilities, no, because others have a weather normalization reserve as well, so on a relative basis, we're equal.
MR. JOHNSON:
Q. You're talking about other jurisdictions in Canada?

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MS. PERRY:
A. I am.
MR. JOHNSON:
Q. Not the United States, right?
MS. PERRY:
A. I haven't done a survey of the ones in United States, but I do believe if we go to Appendix B, to Ms. McShane's evidence in which she outlines all of the comparable utilities, within that a number of utilities do have a weather normalization reserve in the United States, yes, or some form of weather variance reserves.
MR. JOHNSON:
Q. But you're also aware that quite a number do not?
MS. PERRY:
A. I believe nine of the thirteen utilities in Ms. McShane's evidence had it and that's all I'm aware of.
MR. JOHNSON:
Q. Well I'll take that up with Ms. McShane, not you. But if you could turn to the answer, again this was a cross aide, which is from the 2008 GRA, CANP-141?

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MS. PERRY:
A. Yes.
MS. GLYNN:
Q. And that will be entered as Information Item No. 12.
MR. JOHNSON:
Q. We asked in that GRA a few years ago to provide a table basically setting out adjustments to the weather normalization account and the rate stabilization account was also added as a percentage of return on equity for each year from 1986 to the present, along with any appropriate commentary. And a table was provided showing adjustments to the weather normalization account and the rate stabilization account as a percentage of return on equity for the period 1986 to 2006, and it shows that the total adjustments express as a percentage of return on equity vary from a negative 11.2 to a positive 11.6 and it points out an average for the entire period of one percent. But if we see on the chart next to it or following it and I appreciate this just brings us up to 2006, but it would save having to ask you to do it

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again, but you do see, for instance, 2004, 2005, 2006 some significant balances there in the weather normalization. So that would be a significant issue for volatility of earnings, at least on a year to year basis, right?
MS. PERRY:
A. Yes, I would agree, which is why we applied and we have a weather normalization account.
MR. JOHNSON:
Q. And the earnings volatility is another way of saying, you know, your earnings are up and down in a particular year on account of something like this, and would--if Newfoundland Power did not have this weather normalization protection, its risk would go up as an investment?
MS. PERRY:
A. Again, relative to other utilities with the weather normalization reserves that have, would have similar sales profile like Newfoundland Power, yes, everything else being equal, I would agree that the weather would factor into the volatility in Newfoundland Power's sales and hence earnings.
MR. JOHNSON:

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Q. Regarding PEVDA, the PEVDA account came into force January 1st, 2010, do you recall that?
MS. PERRY:
A. Yes, that is correct.
MR. JOHNSON:
Q. And prior to PEVDA, Ms. Perry, I think you will confirm that Newfoundland Power was at risk for any degree of variability and/or predictability that was associated with forecasting pension expense, correct?
MS. PERRY:
A. Yes, I would agree; however, as we laid out in the 2009 evidence, the predictability of the pension expense had changed substantially from where it was prior to 2008.
MR. JOHNSON:
Q. Okay, and you did point that out in the last case, but in terms of the variability that existed prior to that account's establishment, that variability could arise, I take it, from falling or a rising pension asset values, right?
MS. PERRY:
A. Yes, that is correct.
MR. JOHNSON:

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Q. And changes in the discount rate as well, right?
MS. PERRY:
A. Yes.
MR. JOHNSON:
Q. Okay, and how would the forecasting of pension expense be impacted by the falling or rising pension asset values?
MS. PERRY:
A. Just so I understand the question, Mr. Johnson, how would the pension expense be impacted?
MR. JOHNSON:
Q. How could the forecasting of the pension expense be impacted by falling or rising pension asset values?
MS. PERRY:
A. Well certainly if we forecast forward our pension expense, we take the best available information we have, which would be the most current discount rates and the current earned return on those assets for that particular year, we would then look to the future, with future discount rates and the expected return on the assets and apply that to determining

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the forecast pension costs for the upcoming year.
MR. JOHNSON:
Q. And in terms of--and so the rising or falling pension asset values, that was always there prior to discount rate variability, right?
MS. PERRY:
A. Yes, but I would state that 2008 was a big hit to the return. We lost 16 percent in 2008, so we had not experienced that prior.
MR. JOHNSON:
Q. But there's been years, I'm sure, in the past where there's been sizable losses and sizable gains.
MS. PERRY:
A. I would have to check way back in history, but certainly not in my recollection.
MR. JOHNSON:
Q. Could I turn you to -- I won't turn you there, I'll just reflect it for the record. The Commissioners can read it at some point. But in CA-NP-596 I asked Newfoundland Power to please quantify -- well, we can go there. I asked Newfoundland Power to quantify in dollar terms the amount of risk that Newfoundland

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Power was exposed to for each of the five years prior to the PEVDA and then I was told that Newfoundland Power has never performed an assessment on the basis requested. So I've got another aide that we can go to that might shed light on this. And Ms. McShane (sic), this -- oh, I'm sorry, Ms. Perry. Ms. Perry, is there any doubt, I mean, are we really in any dispute at all that the PEVDA did reduce risk that Newfoundland Power previously had been subject to?
MS. PERRY:
A. Mr. Chairman, during the last rate case when we applied for the PEVDA, circumstances had changed. Prior to that period, the volatility in discount rates just simply wasn't there. We saw a two percent movement in discount rates in one year in 2008. So we had not seen those movements prior. So, not having that level of volatility with assets and discount rates, you're given an opportunity to project forward with some reasonable basis. But in 2008, and hence when we came forward in 2009, the world had substantially changed with respect to the volatility with discount rates.

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So I'm not sure that I will agree that I was exposed to the same level of risk because the risk wasn't there prior. This variability wasn't there prior to this time period.

MR. JOHNSON:

Q. But there was certainly -- there was still certainly forecast risk prior to that volatility of some degree, but -

MS. PERRY:

A. Certainly.

MR. JOHNSON:

Q. - but now, Ms. Perry, you confirm for us that that risk has been totally eliminated, right, by the PEVDA?

MS. PERRY:

A. Currently, yes, I would agree.

MR. JOHNSON:

Q. Right.

MS. PERRY:

A. But again, risk is a relative thing. Pension expense deferral accounts are also common with regulated utilities, so Newfoundland Power is certainly no more or less exposed than those other utilities.

MR. JOHNSON:

Q. Who might have them, but I thought that to the extent -- to the extent that there was any risk at all prior to PEVDA on forecasting pension expense, that has been taken away, correct?

MS. PERRY:

A. I will agree with that, yes.

MR. JOHNSON:

Q. And as I pointed out in this CA-NP-596 when I referred, Newfoundland Power was asked to provide that but they've told me they've never performed an assessment on the basis requested, and so I'd like to bring you to another answer from the 2010 GRA which would be Information -- I'm not sure, Ms. Glynn?

MS. GLYNN:

Q. That hasn't been entered yet, so Information Item No. 13.

MR. JOHNSON:

Q. That can be No. 13. That would be the CA-NP-189. Ms. Perry, this table provided the Pro forma transfers to or from the Pension Expense Variance Deferral Account based on the pension expense for each year from 2004 to 2009 and so, for instance, in 2004, $490,000

difference, so the pension expense was a bit higher than the test year pension expense in that year, I take it?

MS. PERRY:

A. Yes, that's how this particular RFI was completed. It was completed on the basis that the base was the test year in 2004, yes.

MR. JOHNSON:

Q. Okay. And so, to put the 490 into perspective, if in that particular year, if you had a PEVDA, the 490 would have just been absorbed into the PEVDA and it would not have been an extra expense that Newfoundland Power would have had to meet over test year forecast of the pension expense? Would that be right?

MS. PERRY:

A. Mechanically speaking, I think, yes, that's right. We didn't have a PEVDA then, but if you were to base it off of 2004, yes.

MR. JOHNSON:

Q. And 2005, it was 1.5 million; 2006, but there might be some early retirements captured into that as well, I would take it, early retirement packages. Would that be right?

MS. PERRY:

A. Yes, the pension numbers, Mr. Chairman, that you're looking at here, the pension expense numbers, are inclusive of an early retirement program that we completed in 2005 and I do recall at the last hearing where we were specifically asked would the PEVDA include changes to pension expense that were within management's control and we advised no at that time, and certainly an early retirement program would be one of those decisions we would make and would be within management's control. So if you are comparing apples to apples, you would have to remove the early retirement program cost from pension expense here because they would not be captured by the PEVDA.

(12:15 p.m.)

MR. JOHNSON:

Q. Well say, 2004, the 490 was not an example of that?

MS. PERRY:

A. No, that was prior to the early retirement program.

MR. JOHNSON:

Q. And that's real money. That's $500,000,

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right? So that's a risk that you no longer have to worry about as Newfoundland Power's CFO?
MS. PERRY:
A. We had the risk. The risk of the exposure was much more limited than what it is today.
MR. JOHNSON:
Q. Okay. But back in 2004, I think your evidence would confirm that the discount rate issue bouncing around, that was not an issue then because that only arose later, right?
MS. PERRY:
A. That was later, yes.
MR. JOHNSON:
Q. Yes. And now, the volatility and discount rates are much reduced, I take it?
MS. PERRY:
A. From what particular point, Mr. Johnson?
MR. JOHNSON:
Q. From the high point before you applied for this PEVDA.
MS. PERRY:
A. We haven't seen the two percent, but I believe they're about three percent lower still since the last time we were here.

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MR. JOHNSON:
Q. Could I turn to the topic of OPEBs, and particularly page 39, and I'm referring in particular to Table 3.6 which sets out OPEBs expense from 2010 to 2014 estimated, and Ms. Perry, we see that the OPEBs expense is forecasted to take about a 1.2 million dollar jump in 2013 and stay pretty close to that number again in 2014. You see that?
MS. PERRY:
A. Yes, I do.
MR. JOHNSON:
Q. Okay. And at footnote 29, which was on the following page, at page 310, it says that "the forecast discount rate for 2013 and 2014 is 4.9 percent and is based on current market indications. The actual discount rate used to value the OPEBs obligation and related annual OPEBs expense is determined at December 31st each year" and it indicates "the approximately 5.6 million dollar increase in OPEBs obligation as at January 1st, 2012 was determined by Mercer, the company's actuaries." What did your actuaries determine to be the discount rate as at December 31st,

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2012?
MS. PERRY:
A. Well, I have yet to go through that, but I've been told that I -- but I have to confirm this because I haven't looked at the assumptions provided by Mercers -- that it's somewhere lower than the 490 and closer to the 450.
MR. JOHNSON:
Q. Okay. So that would -- are you looking to adjust test year expenses upwards then on account of the drop in discount rate?
MS. PERRY:
A. No, the way that it would operate is that changes to OPEB would flow through the OPEVDA or the -
MR. JOHNSON:
Q. So you're not worried about them, but without the OPEBs you would have been worried about them and you would have had to file an update, would you have not, to your evidence?
MS. PERRY:
A. Well, depending on timing and depending on all other cost changes, a consideration would have had to have been made, I will agree. I will also, for the record, note that our pension

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assets in our pension plan -- I've not been through this, but I've been told that the return was higher than our expected return. So therefore, that will be a positive to customers. So we have things that go down. We have things that go up. And you know, you have to sort of consider all of them together before -- without just one thing in isolation.
MR. JOHNSON:
Q. Well, Ms. Perry, what would have been -- or can you put a dollar figure on the expense of the impact of -- if as you say, and this will be subject to confirmation, perhaps you can confirm this by way of an undertaking, what the discount rate would -- the change in the discount rate down to closer -- did you say to 4.5 from 4.9?
MS. PERRY:
A. It's closer to 4.5. I'd have to get the exact number.
MR. JOHNSON:
Q. Okay. And what would that approximate in terms of an increase in the cost of annual OPEBs expense?
MS. PERRY:

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A. If we could go to CA-NP-127? I believe that's our Annual Report and those sensitivities are outlined there. If you could go to the 2011 Report, Chris? And just go on down. Go to the business risk section I believe it is. Go on down. Okay, just one more. Just up one page, thank you. Right here -

MR. JOHNSON:

Q. What page, Ms. Perry?

MS. PERRY:

A. Oh, sorry. What page is this, Chris?

MR. CHRIS WELLS:

Q. 37.

MS. PERRY:

A. So this is -- what's on this chart in the Annual Report is actually the sensitivities for the change in the discount rate assumption and the rate of return on plan assets for the company's main pension plan. So you'll see on the last two lines, the change in discount assumption is really a range of 3.5 to 4 percent, 4.4 percent, for a one percent change in the discount rate.

MR. JOHNSON:

Q. Okay. Can you put that into terms that we can understand in terms of the impact back on the annual OPEBs expense in Table 3.6?

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MS. PERRY:

A. The volatility with respect to OPEBs is more in line with a one percent change in discount rates, is on average about million dollars in OPEBs expense. So if we are -- everything else being equal, if we are decreasing our OPEBs expense from 490 to 450, that's 40 basis points. So it's probably 400,000.

MR. JOHNSON:

Q. Over and above what we see for 2013 expected?

MS. PERRY:

A. For OPEBs, yes.

MR. JOHNSON:

Q. And a similar amount for 2014?

MS. PERRY:

A. Yes, that is correct, assuming all else being equal.

MR. JOHNSON:

Q. Assuming that holds true again. So you say about a half million?

MS. PERRY:

A. 400,000, yeah.

MR. JOHNSON:

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Q. $400,000. And Ms. Perry, in the absence of the OPEVA -

MS. PERRY:

A. OPEVDA.

MR. JOHNSON:

Q. PEVDA, you -- Newfoundland Power, at this stage of the rate application, would most definitely be providing an update from Mercers indicating that the discount rate had gone down and the OPEBs expense has gone up, correct, and filing -- and having the new expected OPEBs expense put into your revenue requirement for the test year?

MS. PERRY:

A. Well actually, this is not completed yet, the 2011, and I believe the assumptions letter from Mercers, the draft version of it, was received a few days ago, so this is new information.

MR. JOHNSON:

Q. It is new, but let us say that the information becomes solidified and it points to a $400,000 increase in OPEBs expense for 2013 -- and I guess you can update us on what it will be while this proceeding is ongoing?

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MS. PERRY:

A. It will be simply just one of our costs though, Mr. Johnson. I guess I have concern about just displaying one cost associated with Newfoundland Power, but yes, we can get that number.

MR. JOHNSON:

Q. Okay. I'm just going to ask an obvious question, Ms. Perry. The obvious question, it seems to me, is that in the absence of the OPEVDA, there'd be no two ways around the fact that if Newfoundland Power was in a general rate application and their actuaries had just told them that discount rate is going up and the annual OPEBs expense was going to have -- or discount rate is going down, so the OPEBs annual expense is going up, you'd definitely be filing an update saying we'd have to change the revenue requirement by the four or five hundred thousand dollars. You wouldn't eat that, would you?

MS. PERRY:

A. I would have to look at in the context of all of our costs. I mean, that's how we would base a decision of whether we would refile a forecast and if it was materially different, then yes, we would consider refiling.

MR. JOHNSON:
Q. And getting to the underlying, one part of the OPEB is the drug benefit for both employees and retirees, correct?
MS. PERRY:
A. That is correct, yes.
MR. JOHNSON:
Q. And your plan reimburses only for the lowest price interchangeable drug unless the physician indicates no substitution. That's what the plan calls for?
MS. PERRY:
A. That is correct, yes.
MR. JOHNSON:
Q. And I have brought before you for a cross-examination aide a document entitled Maximum -- or a printout from the Health and Community Services website.
MS. GLYNN:
Q. That would be Information Item 14.
MR. JOHNSON:
Q. 14. This is an introduction to the Newfoundland and Labrador Interchangeable Drug

Products Formulary that's printed off relatively recently, in January 2013, and this gives background on what the province has done in relation to the formulary. And as I understand it, Ms. Perry, essentially what has happened is that a regulation has been brought in, which is also going to be filed as an information piece. The regulation is brought under the Pharmaceutical Act, as I understand it, and the impact is that the province basically has brought in price controls on generic drugs, right?
MS. PERRY:
A. That is my understanding, yes.
MR. JOHNSON:
Q. Okay. And if we turn to page two of six of that -- oh, I'm sorry, not two of six. It would be page three of six. Actually, I think you should still be back on the -- or maybe you are. No, you are, okay. Keep on going down to where -- there you are. Keep going. Yes. And essentially, they've set out in this information document what the regulation states and it states that "the price for a product listed in the formulary shall not

exceed the maximum price as set out in the following table as of the applicable dates" and I understand that this came into force of law in April of 2012, April 16th, and it says "from April 16th, 2012 to September 30th, 2012, the maximum price to be charged is 45 percent of the brand name price" and then from October 1st, 2012 to March 31st, 2013, it drops, 40 percent of the brand price would be the maximum allowed, and April 1st, 35 percent of the brand price, and Ms. Perry, I asked a question of Newfoundland Power when I was made aware of this, which was late in the day, I have to confess, about whether this would be taken into account in Newfoundland Power's 2013 and 2014 OPEBs expense and before turning to the reply, will it be reflected in the test year requirements, this change? Because presumably it'll mean that the cost will be going down under this price control legislation.
MS. PERRY:
A. So in the response to the question that the Consumer Advocate had with respect to would this impact our -

MR. JOHNSON:
Q. CA-NP-683. I guess we might as well go there.
(12:30 p.m.)
MS. PERRY:
A. Yes, CA-NP-683. So what this response to the RFI states is that the impact of the regulations will or should be expected to reduce the cost of drugs inside the program. So, the theory, and conceptually this is true, that the less you have to pay for drugs, then the lower your health care trend rate should be, all else being equal. So I had a further discussion with our actuaries which provide the long term health care trend rate and the answer wasn't a surprise in the fact that the health care trend rate, as stated here, is based on historical claims experience, expectations related to aging, drug consumption, long term expectations for future drug costs. So this is one variable inside. All else being equal, I will agree that the health care trend rate should come down. The discussion with Mercers and actually with Blue Cross, and I had a further conversation with them, about the practicality, I guess, of

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trying to summarize the impact that this could have on our health care trend rate and they basically say that it's just simply not practical to forecast the impact because we have no claims experience. We have no proof, for lack of a better word, as to what this legislation is actually going to mean for our plan. And so it would, I guess, be premature to reduce the health care trend rate at the expense of having to really increase it by a further amount in the future, if in fact it's not going to result in a reduction in our health care trend rate. So the approach is going to be that we will monitor our results and hopefully it will reduce our costs and if it reduces our cost, it will be reflected in our OPEBs expense and that will be reflected through the OPEVDA again.

MR. JOHNSON:

Q. But I guess the -- all other things being equal, this would be expected to reduce the actual OPEBs cost in 2013, 2014? Would that be a fair statement? Because of the introduction of the legislation.

MS. PERRY:

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A. There are many moving parts, because obviously if 2013 and '14 are high price increases with the drugs themselves, regardless of what percentage you pay, the drug cost may actually go up. So again, there's many variables and judgments that are applied when you look forward. So one of the best indications of where the rate is going is based on experience and Mercer's view that it's, from a timing perspective, it's premature to actually project what this is going to mean to us, and just to put it in context, about 60 percent of our plan is geared towards generic drugs roughly today, and this legislation applies to a percentage of those generic drugs. So it's not even applying to all of our drugs. It is a list of drugs, but it's not applying to all the drugs with inside of our plan. But all things being equal, I hope that this will tend to reduce health care trend costs and that will be reflected in future OPEBs expense and that will certainly return to customers when that happens through the OPEVDA.

MR. JOHNSON:

Q. So the numbers that we are using for your

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OPEBs expense for 2013E and 2104E when -- in Table 3.6, those numbers were developed when?

MS. PERRY:

A. Around August, September when we filed.

MR. JOHNSON:

Q. And when were you aware of the legislation?

MS. PERRY:

A. Well, I wasn't aware until the RFI, but the plan administrator was aware of it and our service provider, which was Blue Cross, actually implement -- it's automatic that they get these legislation changes and so it was implemented inside of our plan in April.

MR. JOHNSON:

Q. When -- how long are the actuaries saying it will take -- I mean, let's put it this way. If this information had been known to them say last year, presumably this number for 2013 and 2014E would be different than what we're seeing now. We presume that because there's been a change, I take it, right? I mean, how much time would be required to figure it out?

MS. PERRY:

A. No, I -- my conversation with Blue Cross, because I asked that, when will we start

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seeing potentially -- it would still be hard to have a linear relationship because so much goes on inside of a plan, but how long would it take, and he said, you know, it probably would take a couple of years because, you know, it's the take up of the drugs, the nature of the drugs, just trying to get some trend lines with the usage and the cost of the drugs. And I believe the 4.5 is also not an absolute number. It's within a range of return which is the health care trend rate assumption. So, I think if we start to see trends that are lower than that, we'll bowl to reducing the trend over the next several years. But I suspect it'll take a couple of years.

MR. JOHNSON:

Q. Have you received anything in writing from Mercers indicating what their opinion is in terms of quantification at this time of the changes, of the effect of the regulation?

MS. PERRY:

A. Mr. Chairman, I asked Mercers to provide me their opinion and the response that we provided in CA-NP-683 is substantially

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confirmed with Mercers that it was unpractical to quantify at this time.

MR. JOHNSON:

Q. Did they provide a letter or a report in that regard?

MS. PERRY:

A. No, they did not.

MR. JOHNSON:

Q. It was just a telephone call?

MS. PERRY:

A. It was a telephone call. I'm not sure if they followed up with an e-mail to confirm, but it was a telephone call.

MR. JOHNSON:

Q. With respect to the issue of credit ratings, Ms. Perry, you indicated when you testified on direct at page 152 -

MS. PERRY:

A. Where are we? Oh, on testimony, okay.

MR. JOHNSON:

Q. You testified that -- starting at the bottom of 151, "I would be surprised if Moody's or DBRS were to indicate an appropriate level of ROE for Newfoundland Power one way or the other" and then you say "what Moody's has

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indicated quite clearly is that Newfoundland Power's financial metrics are somewhat weaker than those of its peers which they state are Fortis Alberta, Connecticut Light and Power, Orange and Rockland Utilities in New York and Public Service Electric and Gas in New Jersey." And Ms. Perry, but you did not go on to say however that Moody's has not expressed any concern about that, right? I mean, that's normal that your metrics have been less than those peers?

MS. PERRY:

A. I'm not sure I would call it normal, but it's certainly been existing for a while, yes.

MR. JOHNSON:

Q. But it's not a concern of Moody's?

MS. PERRY:

A. I wouldn't go as far to say it's not a concern. The fact that they mention that we are weaker than our peers is obviously an item of interest to Moody's.

MR. JOHNSON:

Q. Can I turn you to the Moody's July -- 19 July 2011 opinion at Exhibit 4?

KELLY, Q.C.:

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Q. Towards the end, Chris.

MR. JOHNSON:

Q. And I'm at the -- although the page is not numbered, it's the second page in under the paragraph "modestly weaker financial metrics expected in future." And this is where, as you correctly point out, they state that "Newfoundland Power's ratios continue to be somewhat weaker than those of other BAA rated peers -- BAA1 rated peers, predominantly engaged in transmission and distribution such as Fortis Alberta Inc., FAB, a sister company, Connecticut Light and Power, Orange and Rockland Utilities and Public Service Electric and Gas Company. We expect Fortis Alberta to generate cash flow plus interest to cash flow, interest coverage in the four times range and CFO pre-working capital to debt of about18 percent going forward. CLP, O&R, PSE&G have reported cash flow interest coverage in the four times to five times range" et cetera. And then they say "in contrast, we expect Newfoundland Power to generate cash flow interest coverage in the low three range and cash flow to debt in the 15 percent to 17

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percent range. These figures are modestly weaker than Newfoundland Power's 2010 results and reflect, in part, Newfoundland Power's 2011 allowed ROE of 8.38, down from 9 in 2010."

So when I heard you state that in your direct, I thought that Moody's had expressed some concern, but clearly they're not expressing any concern about that, right?

MS. PERRY:

A. As I said, they're indicating that we're already lower than our peers and they expect us to be a certain range, but we're already lower than our peers, yes.

MR. JOHNSON:

Q. And that's their expectation. You've been lower than your peers for a while. I mean, I remember having this discussion with you back in the last rate case, right?

MS. PERRY:

A. Yes, and the proposal in this application, in my view, puts us pretty square into where Moody's is saying we should be, because our CFO to interest is 3.4. They're saying low threes. And they're saying CFO to debt, we

expect to be in the range of 15 to 17 and our proposal is 16.4. So I think we're square into what they expect us to achieve.
(12:45 p.m.)
MR. JOHNSON:
Q. Well, in fact, Ms. Perry, if you turn to your evidence at Exhibit 3, keeping in mind what they said that we expect Newfoundland Power to have cashflow interest coverage in the low three times range -
MS. PERRY:
A. Sorry, where are you, Mr. Johnson?
MR. JOHNSON:
Q. I'm just reminding ourselves that they say, "In contrast, we expect Newfoundland Power to generate cashflow interest coverage in the low three times range, and cashflow to debt in the 15 to 17 range". Just turn over to Exhibit 3 for 2013. It seems to me that that indicates that in 2013, even without any rate increase at all, in line 38, cashflow to interest is 3.2, and cashflow to debt is 15.5, so that would still meet Moody's criteria, correct?
MS. PERRY:
A. Yes, but certainly, Mr. Chairman, I'll

acknowledge that it's on the low end of the range and that's not necessarily the place that you try to operate the business at, which is a downward slope of matrix.
MR. JOHNSON:
Q. But my point being that they said cashflow interest coverage in the low 3 range, and cashflow to debt in the 15 to 17, and I'm just telling you the 2013 E establishes that, correct?
MS. PERRY:
A. I will agree, and I will agree that if you look to 2014, we're down to 3, and 13.7, which is below the level indicated by Moody's.
MR. JOHNSON:
Q. As a matter of fact, there's hardly any difference between 2012 and 2013 at all, from the point of view of those matrices, and 2012 was a year completely consistent with your financial integrity, was it not?
MS. PERRY:
A. Yes, we've maintained our credit ratings, I will agree.
MR. JOHNSON:
Q. Yeah. If you could turn back to Exhibit 4,

and I think, actually, for 2014E on Exhibit 3, we still see cashflow to interest times coverage, assuming that there's no rate relief at all granted, of cashflow to interest coverage of 3, okay. Mind you, cashflow to debt is a little -
MS. PERRY:
A. Are you back on Exhibit 3? Sorry, I was -
MR. JOHNSON:
Q. Yeah, I just wanted to remind ourselves for a second.
MS. PERRY:
A. Okay.
MR. JOHNSON:
Q. 2014E shows cashflow to debt of 3 times, and cashflow to debt of 13.7.
MS. PERRY:
A. Yes.
MR. JOHNSON:
Q. And in Moody's now at Exhibit 4, what could change the rating down - there you go. Moody's say, "We consider a downward revision of Newfoundland Power's rating to be unlikely in the near term. However, Newfoundland Power's rating would likely be downgraded if

we perceived a meaningful reduction in the level of regulatory support, combined with weaker liquidity and a sustained deterioration of Newfoundland Power's financial matrix, such as cashflow interest coverage of less than 2 times, 2.6 times, cashflow to debt in the low teens", and I think RCF, that's free cashflow to debt below 9. Now Ms. Perry, it's obvious that when I read that, that even 2014 without an ounce of rate relief, you're above cashflow interest coverage of 2.6; in fact, you're at 3, and you're just getting into the low teens in cashflow to debt.
MS. PERRY:
A. So back to the Moody's report where it says, you know, credit downgrade could be possible with a perceived meaningful reduction in the level of regulatory support, combined with reduced matrix, well, these matrix are, while not outside the range - well, one is outside the range because 13.7 is pretty well -
MR. JOHNSON:
Q. I grant you, that's a low teen.
MS. PERRY:
A. It's a low teen. So, you know, one is out,

and the other is deteriorating, and we are earning a regulated return on equity of 6. 89 percent on that basis. So I would have concern that in this situation Moody's would evaluate that the regulated utility is permitted to earn a return of 6.89 percent in relation to all other utilities earning something above that, so it would be the lowest in the country, combined with these weaker financial matrix, is exactly why I would address that I would have serious concerns that this would impact Newfoundland Power's financial integrity.

MR. JOHNSON:

Q. And I grant you that that's not going to be the outcome, but it's illustrative of something, and that is in terms of that cashflow interest coverage of less than 2. 6 times that Moody's talks about, and they'd have to see that on - they'd have to see that on a sustained basis, and you wouldn't even get there if this Board decided to throw out your entire case and say come back in 2015, and you had to survive on the current rates.

MS. PERRY:

A. Which, Mr. Chairman, would be a 6.89 percent rate of return on common equity.

MR. JOHNSON:

Q. And I'm not advocating that.

MS. PERRY:

A. No, but that's what the result is right here for 2014. So you've got to take one with the other, and I think it's all considered in Moody's evaluation of how this utility is set up for the future. So you can't just look at matrix in isolation of the full context of how Newfoundland Power and what Newfoundland Power could earn in that particular year.

MR. JOHNSON:

Q. No, no, I think we're okay on that, and I take it that there is no contest here between us that Moody's is talking about a two-pronged approach. They'd need to see not just a reduction in the level of regulatory support, but a meaningful reduction in the level of regulatory support, and then combine that with a sustained deterioration, because that's what the document says, and you'll agree that that's what the document says?

MS. PERRY:

A. I agree that's what the document says.

MR. JOHNSON:

Q. And do you make presentations to Moody's and the bond rating agencies?

MS. PERRY:

A. Yes, I have discussions with them and we try to meet at least once a year.

MR. JOHNSON:

Q. So in Moody's case, this is the last credit opinion?

MS. PERRY:

A. Yes.

MR. JOHNSON:

Q. When did you last meet with Moody's?

MS. PERRY:

A. I had a discussion with them the latter part of August prior to filing this Application.

MR. JOHNSON:

Q. Okay, and did that discussion happen on the telephone?

MS. PERRY:

A. Yes, it did.

MR. JOHNSON:

Q. And so do you provide them a presentation of Newfoundland Power's case, I mean, in terms of

- you must provide them with a presentation in paper, in writing?

MS. PERRY:

A. Not in 2012. They had certain changeover in their staff, which is why I had a telephone conversation with them in August. The plan will be that once we understand the outcome of this particular rate case, because rate cases are pretty significant to credit rating agencies, that we will arrange a time to meet with both DBRS and Moody's and walk them through the order and the impact that it will have on Newfoundland Power.

MR. JOHNSON:

Q. Yes, okay, and Ms. Perry, do you sit down with the rating agencies separately in that process, I take it?

MS. PERRY:

A. Oh, yes, yes.

MR. JOHNSON:

Q. And would they come to St. John's for that or would you go to where they are?

MS. PERRY:

A. Unfortunately, they haven't gotten to St. John's. I usually got to go to Toronto, yes.

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MR. JOHNSON:
Q. And so when was the last time you made a presentation to either DBRS or Moody's?
MS. PERRY:
A. I would have to confirm, Mr. Johnson. I don't believe it was in 2012, and as I said, the credit rating agencies went through a - certainly a bit of turnover inside of the agencies themselves, so we just never - the meetings never happened in '12. I would have to confirm when it was in 2011.
MR. JOHNSON:
Q. And so - and when you go up there, you don't go up there without a presentation to give them, a written presentation?
MS. PERRY:
A. I believe the last time I was there, I did have a few slides that I did walk them through, yes.
MR. JOHNSON:
Q. And would you still have those slides?
MS. PERRY:
A. I'd like to say yes, but I'm not sure.
MR. JOHNSON:
Q. Would you be able to undertake to provide us with your most recent presentations to each of DBRS and Moody's?

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KELLY, Q.C.:
Q. I'll take that under advisement, Mr. Chairman, for consideration.
MR. JOHNSON:
Q. Well, we can - you want to consider whether or not you're going to object to that?
KELLY, Q.C.:
Q. I'm going to consider, (a) what there is or isn't, and I'll advise you as to what the position we take with respect to it. I'm simply reserving the position, Mr. Chairman.
MR. JOHNSON:
Q. Okay, all right. Well, perhaps what we could do is look at it in the anon. Similarly, would you keep minutes of the meetings, Ms. Perry?
MS. PERRY:
A. No, there would be no minutes.
MR. JOHNSON:
Q. Let me turn to the AAF. Ms. Perry, in the last General Rate Application, you indicated that the Board's ROE formula until around that time had been giving fair and reasonable returns on equity, and in the Board's decision at PU-43, page 13, I'd just like to bring you to the extract for a second. PU-43, and I'm on the wrong page here, I think.

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MS. GLYNN:
Q. It was filed as consent exhibit this morning, but you had to get it from the website yesterday.
MR. HAYES:
Q. We can get that on the screen. We're just going to have to hook up the internet again.
MR. JOHNSON:
Q. I'm looking for the paragraph -
MR. HAYES:
Q. That's the reasons for decision, Mr. Johnson?
MR. JOHNSON:
Q. Yes, and I wish I could find the paragraph that I was going to try to bring you to. Yes, I see it. If I could bring you to page 28 of the Board's decision, particularly line 5. The Board stated in the passage from line 5 to line 12, "That Newfoundland Power bears the burden of showing that it is appropriate to discontinue the use of the automatic adjustment formula, a well established regulatory tool that was expected to be used to set rates for Newfoundland Power in 2010. The Board is not persuaded by the evidence of Ms. McShane as to the historical under-performance of the formula, especially given the evidence of both Ms. Perry and Mr. Ludlow that the automatic adjustment formula established appropriate rates of return on rate rates for almost a decade until the extraordinary financial market conditions which developed late in 2008". Ms. Perry, in 2009, what was it that had led you to judge that the automatic adjustment formula no longer gave fair and reasonable ROEs? Was it the fact that the long Canada yields were falling, and with them the fair ROE at a time when corporate borrowing costs were also increasing?

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MS. PERRY:
A. Yes, that was a factor, no doubt, that the operation of the formula was producing unfair returns, and I believe around that time a couple of other regulatory jurisdictions had suspended the formula as well, which, you know, regulatory consensus on the formula was

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becoming weaker around that time.
(1:00 p.m.)
MR. JOHNSON:
Q. And there was a concern, I believe, about the corporate borrowing cost increasing at the same time?
MS. PERRY:
A. Yes.
MR. JOHNSON:
Q. And we will be taking this up with Ms. McShane, and Dr. Booth will be talking about it as well, but are you aware that Ms. McShane recommended an ROE adjustment formula in an Enbridge Line 9 hearing before the National Energy Board in 2010, and again in a Gazifere hearing before the Regie in 2010, and in both cases she supplemented the standard formula with a 50 percent adjustment to credit spread changes? Are you aware of that?
MS. PERRY:
A. I am aware. I haven't been through it in detail, no.
MR. JOHNSON:
Q. Can I take you to Dr. Booth's testimony at page 68, and this is part of a discussion in

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Dr. Booth's report where he addresses how he would enhance the adjustment models since so many were suspended, and he sets out the long term Canada from 1995 to 2010, and he sets out the spread between, I believe, the "A" spread using Scotia Capital's index, and, I guess, the utility bond spread, and then he reports what the NEB formula would produce and he talks about what his suggestion would have produced over that period. On the next page, he graphs the results of the standard National Energy Board formula and his enhancement to it, but you can see that for 2009, it would have awarded a fair ROE of 9.39 percent, versus the actual NEB's formula of 8.57 percent, or about 55 basis points more. Do you see that?
MS. PERRY:
A. Yes, I do.
MR. JOHNSON:
Q. And this Board for 2010 decided that a fair and reasonable return for Newfoundland Power was 9 percent, correct?
MS. PERRY:
A. That is correct, yes.

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MR. JOHNSON:
Q. Okay, and do you regard the 8 basis point difference, that being the difference between what the Board ordered at 9 percent, and the 8.92 percent that Dr. Booth's enhanced NEB formula would have allowed, do you regard the 8 basis point difference as being material?
MS. PERRY:
A. For clarification, Mr. Johnson, Dr. Booth's display of numbers here, and that would have applied to the NEB formula, is it?
MR. JOHNSON:
Q. He's adjusted, I think, to add a credit spread. That's my understanding. He'll be able to speak to it more fully than I, but he's put a gloss, I guess, on the NEB formula and he ends up with a higher number than the NEB, say, for 2010.
MS. PERRY:
A. But my question is in terms of the parameters used in the formula, they're the parameters of the NEB, is it, and not Newfoundland Power, is what I'm suggesting.
MR. JOHNSON:
Q. Okay.

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MS. PERRY:
A. Yeah.
MR. JOHNSON:
Q. Okay, well, I want to be careful I don't get in over my waders a great deal on that topic.
MS. PERRY:
A. Yeah.
MR. JOHNSON:
Q. And perhaps what I - I was planning, in fact, to confer further with Dr. Booth, who's flying back and forth today, because I wanted to confer with him prior to closing testimony with Ms. Perry, in any event, so what I think I'll do is take that under advisement and make sure that what I'm putting to you is what he would intend for me to put to you. Ms. Perry, I guess you'll know that it's getting late in the day when we're talking about depreciation, I saved that for last. At page 163 of the transcript when you testified on direct, at the bottom of page 162, going up to 163, having been asked, "What financial impact will the consumer advocate's proposals have on customers", the answer is that, "Well, a prominent feature of the consumer advocate's

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depreciation proposals include the transfer of approximately 70 million dollars net of tax that has been collected from customers in the past to the customers in the future", and I take it you're not implying in any way that there is a 70 million dollar revenue requirement impact in this case, are you?
MS. PERRY:
A. No, not at this rate proceeding. My point was that we are fundamentally taking 70 million that has been collected and incorporating that into lower depreciation rates going forward, which ultimately means it has to be collected from future customers again at some point in the future.
MR. JOHNSON:
Q. You go on to state, "The proposals have the short effect", or I take it you meant the short term effect -
MS. PERRY:
A. Yes.
MR. JOHNSON:
Q. "Of reducing annual depreciation expense and the revenue requirement by approximately 10 million dollars". What time frame are you

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referring to when you state that it'll have a short term effect?
MS. PERRY:
A. If we could go to CA-NP-320. This RFI was filed in response to the expected crossover, I guess, of when the revenue requirement associated with moving to ALG would actually be higher than ELG, and for reasons that are pointed out in this RFI, there's many variables that impact the crossover period, being rate base growth, in terms of what plant account you're looking at, the estimates for retirement and net salvage, and - but we did take an account to illustrate and the crossover was 11 - Chris, if you could just go down a bit further, please. So with the 2 percent rate base growth analysis, the crossover point was at 11 years.
MR. JOHNSON:
Q. And at a net plant growth rate of 4 percent, the crossover point is 15 years, I think the response says.
MS. PERRY:
A. Right, for this account, yes.
MR. JOHNSON:

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Q. For this account, and would 11 and 15 years, would that be considered short term in Newfoundland Power's judgment?
MS. PERRY:
A. Well, I think in response to this RFI, we were trying to make a couple of points. One is that it is 11 years, and so it's not 30 years, and the other point is that - and this is an estimate based on one plant account. So based on, I guess, what actually happens in the future, it could be a little bit more, could be a little bit less. The point here is to illustrate that upon moving to the ALG methodology, yes, customer's revenue requirement or the revenue requirement associated with depreciation will be lower for a specific period, but not for a long period. I mean, it's 11 years on this one account, and then customers are going to be paying more, and I'll also make a point here that - and throughout those 11 years, Newfoundland Power's rate base is actually growing and the return on rate base is actually growing, and the crossover point is estimated to be 11 years.

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MR. JOHNSON:
Q. And would you take issue that the governing principles would be principles such as inter-generational equity and the matching principle of cost to when the service is rendered? I mean, that would be the - that would be the principles through which this matter should be determined?
MS. PERRY:
A. I think it's one of the big considerations in the fact that the ELG methodology being a more precise methodology, I guess, with respect to breaking out equal life groups, that based on the expert advice from Gannett Fleming that it does match the consumption of the asset with the use of the asset, so it's a better matching certainly of the cost of today with the customers of today, yes. So it certainly is - it is a consideration.
MR. JOHNSON:
Q. Okay, I think - I'd like to break now. I may have a small bit more for Ms. Perry in the morning, but I'm - if the Chair is fine with it, I'm certainly prepared to yield to my learned friend, Ms. Greene, to ask some

questions prior to me going back to Ms. Perry.

MS. GLYNN:

Q. Mr. Chair, we have a couple of options at this point. We do note that Ms. Perry will have to return tomorrow. Ms. Greene has indicated that she has about a half hour of questioning, so we could take a five minute break now and complete that half hour, or we could break for today and complete Ms. Perry tomorrow morning. There would be Ms. Greene, any follow-up by Mr. Johnson, and then, of course, any follow-up by Newfoundland Power tomorrow morning for Ms. Perry.

CHAIRMAN:

Q. Why don't we forego the break and carry on? Do you want to do that?

MR. JOHNSON:

Q. That's fine with me.

CHAIRMAN:

Q. Anybody vehemently opposed to that? If you are, let me know. I'm not sensitive.

MS. GLYNN:

Q. Board staff, and I think the witness would appreciate a quick break before we continue on for the next half hour.

(1:13 p.m.)

CHAIRMAN:

Q. Well, I'll defer to the witness. We'll break.

MS. GLYNN:

Q. Thank you.

(RECESS)

(RESUME - 1:25 P.M.)

CHAIRMAN:

Q. Okay. Go ahead, Ma'am.

MS. JOCELYN PERRY - EXAMINATION BY GREENE, Q.C.:

GREENE, Q.C.:

Q. Good afternoon, Ms. Perry.

MS. PERRY:

A. Good afternoon.

GREENE, Q.C.:

Q. The first area that I wanted to speak with you about is your forecast that you used with respect to your Application. You filed the Application on September 14th of 2011, is that correct?

MS. PERRY:

A. Yes, that is correct.

GREENE, Q.C.:

Q. And at that time you provided a forecast of your 2013 and your 2014 test year requirement

as well as the forecast for 2012, is that correct?

MS. PERRY:

A. Yes, that is correct.

GREENE, Q.C.:

Q. What was the date that was used for actual information in preparing the forecast? You must have had a cut off date for actuals. What was that date?

MS. PERRY:

A. I believe it to be June, but that would be subject to check. I believe it was June.

GREENE, Q.C.:

Q. So we have - in your forecast for '12, '13, and '14, we have actual data for '12 to June, you believe?

MS. PERRY:

A. To June, yes.

GREENE, Q.C.:

Q. If we could go for a moment, please, to CA-NP-409. You did touch on this issue to a certain degree with Mr. Johnson, and Mr. Johnson or the consumer advocate asked in this information request as to whether you planned or expected to update your forecast in this

proceeding, and the answer in the RFI CA-NP-409 was that you did not plan to update those forecasts?

MS. PERRY:

A. That is correct.

GREENE, Q.C.:

Q. And my question is, is that - does that continue to be Newfoundland Power's position?

MS. PERRY:

A. Yes, it is.

GREENE, Q.C.:

Q. You're presently in the middle of year end for 2012, and I expect you will be getting back to it as soon as your evidence is over, but at this point in time seeing that you must be well into your year end preparation for 2012, are you aware as Chief Financial Officer of any material change in any of the significant inputs into your 2012 forecast which would materially impact your 2012 forecast and your 2013 and 2014 test year forecasts that have been filed with this proceeding?

MS. PERRY:

A. No, I'm not aware of anything material, with the exception of the decrease in the discount

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rate as I referred to earlier with respect to the company's defined benefit pension plan and its OPEB plan, and I will also note that I'm not sure of the impact because there's countering impacts to the discount rate with asset returns, but I haven't had the privilege of actually looking at those numbers just yet.

GREENE, Q.C.:
Q. So with the exception of that one issue, you're not aware of a material change in any other of your significant cost categories, such as labour costs or operating costs?

MS. PERRY:
A. No, I'm not aware, no.

GREENE, Q.C.:
Q. I wanted to talk to you a little bit about the automatic adjustment formula, and I just wanted to summarize what I understand is the company's position to ensure that I've understood it correctly. Newfoundland Power's position is that the formula should be eliminated, not suspended for a period of time, but completely eliminated?

MS. PERRY:
A. Yes, our proposal was to discontinue.

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GREENE, Q.C.:
Q. And I know you've talked a little bit with Mr. Johnson about this, but again not to till that ground again, I want to summarize what I took from some of that discussion, the primary reason, as I understand it, is the current unsettled financial market conditions, is that correct?

MS. PERRY:
A. That is correct, yes.

GREENE, Q.C.:
Q. I want to talk a little bit now about what happens if there is no formula. The company's position is throw out the formula, we would go back to having no formula, back to prior to 1999, I believe. In the future, if the Board agreed with the company's position, how would the ROE be changed in the future, the return on equity for the company?

MS. PERRY:
A. In the absence of a formula, and in line with Newfoundland Power's proposals, we've proposed that the cost of equity as determined in a General Rate Application would actually stay into effect until the company's next General

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Rate Application, recognizing that general rate proceedings usually happen every two to three years, so the time span is certainly not long, and also recognizing that at any point in time in the intervening period, the Board can certainly call upon Newfoundland Power to file cost of capital evidence if, in fact, financial markets warranted such a change. So our position is that the proposed cost of equity in this proceeding would stick until the next general rate proceeding.

GREENE, Q.C.:
Q. So in that particular case, unless the Board took some extraordinary action, it would remain within the discretion of Newfoundland Power as to when to apply to readjust either the return on equity or another - or rates, so a general rate application, is that how I understood your answer?

MS. PERRY:
A. Yes, I would agree with that, but again the Board certainly would have the authority to call Newfoundland Power in at any time.

GREENE, Q.C.:
Q. In the information that's been filed with your

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Application, there's an indication of a revenue shortfall for the company in 2015.

MS. PERRY:
A. Yes.

GREENE, Q.C.:
Q. When do you - is that when you currently forecast reapplying to the Board for another general rate proceeding?

MS. PERRY:
A. So certainly if we could go to CA-NP-398. This RFI provides the company's five year financial forecast, and if you turn to page - well, it's called 1 of 9, but it's page 3 in the document, you'll notice that, yes, in 2015, currently the company is forecasting a revenue shortfall of 4.4 million in 2015.

KELLY, Q.C.:
Q. I don't think we're quite on the right page.

MS. PERRY:
A. Oh, sorry, sorry. Go on down, Chris.

KELLY, Q.C.:
Q. You got the right page, just not down far enough. There we go.

MS. PERRY:
A. So on line 34, you'll notice that we are

projecting a revenue shortfall of 4.4 in 2015, and 7.6 in 2016. So as you can respect, the closer you get to that time period, the more certain we'll become of our cost and the revenues and any things that have happened materially within that time period. So based on this, yes, it would look as if we're going to be in front of the Board in 2015, but certainly that observation or final observation and determination will be made as we get closer to it, and it would be premature right now to say that - to confirm that it would be 2015, because many things can change by the time we get to the show.

GREENE, Q.C.:

Q. And in making the determination as to when to file for a General Rate Application, the company looks at its forecast revenues, it looks at the return on equity, and multiple factors, and makes that decision and will only apply generally to increase rates to cover what are forecast shortfalls. Is that generally the way that it occurs?

MS. PERRY:

A. Yes, that's exactly how it happens.

GREENE, Q.C.:

Q. If there were to be a change in the market conditions such that the market would indicate that the fair return for the company is actually lower than what the Board sets in its order, do you think the Board should be concerned about whether there's a trigger or a mechanism to ensure that the utility comes back to address what would be a lower rate of return?

MS. PERRY:

A. I agree in principle, and I guess that's the essence of what the formula was providing from 1998 until 2008. The trouble that I see with the mechanism is that it may actually do the opposite from what it should do. So we may be in a time where a mechanism should be signalling an increase in the rate of return for Newfoundland Power, and the mechanism may actually be signalling a decrease. So in principle, I agree that a formula was meant to provide for regulatory efficiencies between test years and adjust the cost of capital for changes in the financial markets. Given, I guess, what has transpired in the last couple

of years and the status of the capital markets, I would say that that mechanism wouldn't necessarily do what it was intended to do, and hence why we've proposed to discontinue.

GREENE, Q.C.:

Q. Okay. Your concern is when the ROE should increase, and what I would like to talk about first, and I'm going to come to the second one, when the market conditions would indicate that there is a decrease, if there is no formula, how would that issue of concern be addressed from the company's perspective, how should it be addressed?

MS. PERRY:

A. Well, I think it's fair to assume that the Board has the right to call upon Newfoundland Power to provide cost of capital evidence if it feels that it's the right time to review cost of capital for Newfoundland Power at any time. So if it was viewed that the cost of equity was decreasing, and Newfoundland Power's equity should be decreasing as well, then I think the Board does have ultimate authority to call Newfoundland Power in to

evaluate cost of capital.

GREENE, Q.C.:

Q. So it would be left to the Board - nothing would be initiated by the company, in your perspective?

MS. PERRY:

A. I would have to be there to see the magnitude, but I'm trying to envision a time where we'd come in for a lower cost of equity, but I guess it could happen.

GREENE, Q.C.:

Q. But generally it would not be an initiative taken by the company?

MS. PERRY:

A. Right.

GREENE, Q.C.:

Q. We'll come now to the formula that you have suggested that it be eliminated. Again I don't want to review ground that Mr. Johnson has covered, so I'll summarize my understanding of Newfoundland Power's position. I understand that the company believes that the formula worked relatively well until 2008, is that correct?

MS. PERRY:

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A. That is correct.
GREENE, Q.C.:
Q. And that the primary reason that the formula, in your view, did not work properly then was primarily as a result of the financial market conditions with the abnormally low long Canada bond rates, is that correct?
MS. PERRY:
A. That is correct.
GREENE, Q.C.:
Q. And I also understand that with respect to 2009, you did apply for a General Rate Application and we had a new ROE set in 2010 for 2010 by the Board of 9 percent?
MS. PERRY:
A. Right, 9 percent, yes.
GREENE, Q.C.:
Q. I won't go through that discussion where you did not agree with Mr. Johnson that that was fair, that you left that to others, or with respect to 2011, but generally Newfoundland Power did not take any action further with respect to 9 percent or 8.38, and you also agreed, I believe, that your financial integrity was not impacted as a result of

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those decisions, is that correct?
MS. PERRY:
A. That is correct, yes.
GREENE, Q.C.:
Q. So if the formula worked relatively well, I guess the first year, in your view, that it didn't really work well was 2011, is that correct - for 2012, I should say.
MS. PERRY:
A. And I believe it was signalling a return in 2009 that was lower than the return allowed by the Board at that time.
GREENE, Q.C.:
Q. And that's why you applied for the -
MS. PERRY:
A. Right, yes.
GREENE, Q.C.:
Q. One of the principle reasons why you applied?
MS. PERRY:
A. Right, exactly.
GREENE, Q.C.:
Q. And then the next time would have been for 2012?
MS. PERRY:
A. Well, the formula actually operated for 2011,

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and that's when the forecast cost of equity was estimate at 8.38.
GREENE, Q.C.:
Q. Yes, and as I said, I'm not going to go down that road as to whether you believe it was fair or not, but you took no action, you accepted the 8.38 percent?
MS. PERRY:
A. Exactly. and then for 2012, the formula was indicating a cost of equity of 7.85, and then for '13, I believe it was 7.53, so, yes, 2012 and 2013.
GREENE, Q.C.:
Q. And because of your view that 2012 ROE, as indicated by the formula, would produce an unjust or an unfair result, you applied to the Board to suspend the operation of the formula for 2012, is that correct?
MS. PERRY:
A. Yes, that is correct.
GREENE, Q.C.:
Q. And that was approved by the Board.
MS. PERRY:
A. Yes, for 2012, yes.
GREENE, Q.C.:

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Q. So in light of the history of where the formula has worked well or been suspended when it hasn't, I guess I wanted you to explain why you want the formula totally eliminated as opposed to suspended in your Application, and as you know, it has been suspended in other jurisdictions rather than eliminated?
MS. PERRY:
A. Yes, and I do believe it's eliminated in Alberta. I'm not sure, but -
GREENE, Q.C.:
Q. It's been suspended in Alberta.
MS. PERRY:
A. Yeah, okay. With respect to the discontinuing the formula versus suspending the formula, I'm not sure there's a big difference with it. I think that - we're not against the formula, we're not against a formula in specific financial market conditions and we've said that, that we believe that a formula can work in certain financial market conditions, but given that we are in current financial market conditions, discontinuing the formula until financial market conditions resume to pre 2008 where a formula can certainly be considered, I

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guess it's a - it's a fine line with me as to the difference between if we suspend it until then or discontinue it, because the Board can certainly at any point in time put it back on the table for future consideration. So even if it were to be discontinued, the Board can in its authority put the automatic adjustment formula back on the agenda to be discussed in the future when capital market conditions are more normal.

GREENE, Q.C.:

Q. Coming to the formula, there have been changes suggested to the formula. I understand Newfoundland Power's position to be that the recommended changes by two independent experts, one being Mr. MacDonald, and the other being Dr. Booth, are not acceptable, is that correct?

MS. PERRY:

A. Yes, I think that's correct. I mean, I struggled with the operation of the formula and trying to understand the workings of the formula. I respect the fact that the two proposed formulas, given that they are two variable formulas, try to limit the impact on

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the movement in long Canada bond yields, but I'm still, I guess, not convinced that the formula is going to - well, given that there's a lack of a relationship between the movement in long Canada bond yields and that of a utility's cost of equity, that the formula is actually going to signal an appropriate return on equity for Newfoundland Power, even with the two variable formula. So I tried in my direct to just display some of the concerns that we had, given that when bond yields should go up in one case, the return goes in a certain direction, but it doesn't in the other formula. So it clearly shows that both of the formulas are signalling different things. So the relationship between the long Canada bond movements and a utility's cost of capital, I think, are mirrored in these formulas that are proposed.

GREENE, Q.C.:

Q. Did Newfoundland Power do any of its own analysis with respect to possible modifications or changes to the formula that it could suggest to the Board in its Application?

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MS. PERRY:

A. We certainly asked our experts their opinions, and those opinions are on record. We looked to the one formula or the two formulas that exist in Canada, because for the most part, most of the formulas have been either discontinued or suspended, but certainly we did look at the OEB formula which is substantially what's proposed in this proceeding, and so - so there was nothing that, I guess, rose to the surface with respect to satisfying that a valid relationship actually exists between the two, such that any movement between test years are going to be a reflection of a utility's cost of capital, and I think that's where we landed at the end of the day.

(1:45 p.m.)

GREENE, Q.C.:

Q. You said that you asked your cost of capital experts. What experts did you ask with respect to modifications to the formula?

MS. PERRY:

A. That would be Ms. McShane and Dr. Vander Weide.

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GREENE, Q.C.:

Q. Dr. Vander Weide has provided evidence that he did not study a review of changes to the formula and had no position with respect to the formula, that is on the record. Did he provide evidence to Newfoundland Power that is not part of the record?

MS. PERRY:

A. No, just Ms. McShane provided the evidence.

GREENE, Q.C.:

Q. I would like to talk to you about the changes suggested by Mr. MacDonald.

MS. PERRY:

A. Yes.

GREENE, Q.C.:

Q. And during direct evidence, you did file an exhibit called JP-1 and I wonder if we could bring that up, please, for a moment. I just wanted to look at this very briefly because you did take us through it and JP-1 illustrates the change, assuming the base forecast, 3.04 or that is what the base forecast is and that is what is used in the formula to determine a fair return for 2014, if a formula were to be used for 2014, you

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indicated what the current forecast is for 2014 for the long Canada bond yields, is that correct at the 2.59?

MS. PERRY:

A. Yes, that is correct.

GREENE, Q.C.:

Q. Which obviously is a 45 percent change and given one of Mr. MacDonald's recommendations, it is to adjust by half of that to 50 percent change, so that's why we get to 23 percent reduction there. And then in your next, the other suggested change by Mr. MacDonald is to reflect a chance in the utility bond spread, is that correct?

MS. PERRY:

A. Yes, that is correct.

GREENE, Q.C.:

Q. And in this example there's no change in the bond spread, so the ROE does not get adjusted by the formula as a result of a change in the utility bond spread.

MS. PERRY:

A. That is correct.

GREENE, Q.C.:

Q. And when you therefore apply those changes,

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the reduction in the ROE would be .23, is that correct?

MS. PERRY:

A. Yes, that is correct.

GREENE, Q.C.:

Q. However, Mr. MacDonald has proposed a deadband of 25 basis points, so in effect there would be no change in ROE if his recommended proposals are accepted, is that correct?

MS. PERRY:

A. That is correct.

GREENE, Q.C.:

Q. And what I would like to do now is to file an additional exhibit where it has been distributed to the parties, for ease of reference it's been called exhibit JP-1(a), because I believe in your direct evidence, Ms. Perry, you went on to describe what a 6 basis point change would be.

MS. PERRY:

A. Yes, I did.

GREENE, Q.C.:

Q. And we find it a little confusing in following your direct and then actually reviewing the transcript.

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MS. PERRY:

A. Yes, I apologize for that.

GREENE, Q.C.:

Q. So we thought it would be helpful to ensure that everyone understood this, what the concern is, so if we can just work our way through JP-1(a) and this relates back to your direct evidence where you talked about a 6 basis point change, but the 6 basis point change you were talking about was really an additional reduction in the forecast for the long Canada bond yield, is that correct?

MS. PERRY:

A. Yes, it's the difference between the current consensus forecast and if that were to be reduced just be 6 basis points, yes.

GREENE, Q.C.:

Q. Right. And I would like to point out here, at the bottom of this exhibit, JP-1(a), there is a reference you'll see at the bottom with the asterisk, to the transcript and I'd like to correct, we say January 13th, but it was actually January 10th. A mistake in the date at the bottom in the footnote.

So, in this particular case when we see

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that there is an additional change in the forecast versus the base rate that would have been set for 2013, the change then indicated, as a result of the change in the long Canada bond yield is actually 51 basis points, is that correct? Is fifty one percent -

MS. PERRY:

A. Yes, yes -

GREENE, Q.C.:

Q. - because it's 2.53 instead of -

MS. PERRY:

A. Yes, that is correct.

GREENE, Q.C.:

Q. So, of course, this time they propose is that we take 50 percent of that, that the co-efficient adjustment reduces from .8 where it currently now is in the formula to .5?

MS. PERRY:

A. That is correct, yes.

GREENE, Q.C.:

Q. Okay. And again, we have no change in the utility bond spread as you showed on JP-1.

MS. PERRY:

A. Yes.

GREENE, Q.C.:

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Q. This time, however, the increase or the decrease, I should say, is 26 percent which is above Mr. MacDonald's deadband. So, in fact, there would be a reduction in the 2014 ROE for Newfoundland Power, is that correct?

MS. PERRY:

A. Yes, from 8.91 to 8.65 percent, yes.

GREENE, Q.C.:

Q. And I'm going to come back to your concern with how it worked in that situation, but before I do that, I wanted to go through your other example you had used in your direct, which is instead of a reduction in the long Canada bond yield, we had an increase. So here we have filed exhibit JP-1(b) which is just to set out what you had described in your direct evidence. And here you are talking about an increase in the long Canada bond yield verses the current forecast and you used an increase of 75 basis points.

MS. PERRY:

A. Yes.

GREENE, Q.C.:

Q. So here we see when you apply that in the formula, the base forecast obviously is still

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the same, 3.04, the current forecast, however, has now increased from what we saw in your JP-1 by 75 basis points. The difference in the forecast long Canada bond yields is .030 or 30 basis points and if the--and actually Dr. Booth made the same proposal as Mr. MacDonald in this regard that you would adjust based on half of that; in other words, we reduce the co-efficient adjustment from .8 to .5, we see that the reduction there--or sorry, the increase there would be 15 basis points, there would be again no change in the utility bond spread and here because there is, it's within the deadband, you would have no change. So instead of reducing to 8.91 to reflect that increase, there would be no change, it would remain at 8.91 and you would not get an increase because the current forecast had gone up, is that correct?

MS. PERRY:

A. That is correct, yes.

GREENE, Q.C.:

Q. So your concern seems to be around the--is it around the deadband of the 25 basis points and what is your position with respect to the

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proposed change for the--adjusting the co-efficient to .5 and adding on a credit spread adjustment. So we wanted to explore with you the exact nature of your concern, does it relate to the deadband? Let's start with that.

MS. PERRY:

A. No, it's less about the deadband, on the operation of a deadband. It's more--I think it comes back more to the pure relationship of the movement of long Canada bond yields and that of the utility's forecast cost of equity and in this particular example, you're in a situation where if bond yields decrease by 6 basis points, by 6 basis points, the utility's cost of equity reduces by 20.26 percent, so it goes from 8.91 to 8.65, just by a 6 basis point drop.

GREENE, Q.C.:

Q. But when you say that, isn't it actually 51 basis points because it's a change from what the base was used in the formula, verses where the forecast is, so it's not a 6 basis point change, it's a 51 basis point change in the forecast long Canada bond rate from what was

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used to set the base.

MS. PERRY:

A. The--I will take this slow because I know we're trying to explain the numbers. The example that I had given was if nothing changes in the financial market conditions, if nothing changes, then it's reasonable to assume that the long--the consensus forecast would remain the same, so there would be no change in the forecast long Canada bond yield if nothing changes in the market, so the 2. 59 should hold. The 2.59 should hold. Now compare that 2.59 to the base forecast that's in Mr. MacDonald's formula, so if the consensus forecast changes by only .06 or 6 basis points, which is not much and certainly one could argue it's no change in the financial markets, it actually would signal a reduction in our cost of equity. Nothing has changed; whereas in the second example, again, we're now saying we're going to be changing, so the long Canada bond yields are actually going to increase by .75 percent and compare that then to the base, we actually stay at 8.91. So in one case the long Canada bonds are moving substantially from where they are today, which would signal that the financial markets are changing, but yet it's not doing anything for the utility's cost of equity, but back to the first example in JP-1(a), you have a situation where very little is changing, only the forecast consensus bond yield is moving by 6 basis points and the utility's cost of equity drops form 8.91 to 8.68. So as I said, I think the words I used was it appears unbalanced and the relationship between the movements of long Canada bond yields from where they are today are not quite clear in terms of what the formulas are indicating.

GREENE, Q.C.:

Q. But when you look at the formula, you apply the formula, you don't look at it as to where you were when you were in the last rate case, you look at what the current forecast is, so when you look at 1(a) you actually see a change, you see a further reduction, it's 50 basis points. So when you go, you're looking at it into the future and you're saying, okay, there's a 50 basis point spread between what

we--51 basis points between what was used to set the rates and where it is now when we're forward looking. So that's the trouble that we're having when you're comparing it to a current forecast now when the formula talks about the future and you look at the forecast at the point in time that you're setting it, so when you look at it and you have a 51 basis point reduction and there is a--half of that roughly goes as a reduction in your ROE and how the formula works to me it did not seem unreasonable.

MS. PERRY:

A. So I've spent a bit of time on this, just trying to figure out the operation of the formula and what I deduced is the consensus forecast for long Canada bonds that we're using in the formula, the 2.59, is a forward looking estimate over a 30 year long Canada bond yield. The basis upon which cost of equity is determined in a rate proceeding is a forward looking long Canada bond yield. The two are done under different methods and there are two different numbers that will come out of that, so Mr. MacDonald is saying that the

forward looking is 3.04, the consensus forecast is saying 3.--2.59. I think this is exactly my point. I believe the parameters in the formula are not necessarily apples and apples.

GREENE, Q.C.:

Q. Okay.

MS. PERRY:

A. Because if financial market conditions do not change from where they are today, it is quite reasonable to assume that the consensus forecast for long Canada bond yields will remain at 2.59 and that number will be compared to 3.04, right? And that then will precipitate a decrease in Newfoundland Power's cost of equity when there's been no change in the market and I guess that's probably the flaw that I see in the formula.

GREENE, Q.C.:

Q. So we've already had a discussion earlier with Mr. Johnson that both Ontario and in Quebec they did adjust the formula by both the 50 percent--adjusting the co-efficient adjustment to .5 and adding the utility credit spread, so you have expressed your view that that would

not be acceptable to Newfoundland Power, to the company, as proposed changes to the formula even though it has been adopted in other jurisdictions?

MS. PERRY:

A. Yes, that's our position. The 50 percent certainly is a lower co-efficient than the 80 percent, so the relationship between long Canada bond yields and the utility's cost of equity is reduced in the formula, but I guess the essence of what is that relationship is still not clear, I guess, to us and it is possible that this formula could produce an unfair return for Newfoundland Power and as much as we enjoy coming back here to debate cost of capital, you know, to look forward and to think about having to file again in the fall, based on this analysis right here, it's quite possible that we could very well have to do that. So I think from our perspective we haven't been convinced that the relationship is there and that the relationship is going to hold such that the formula actually yields a fair return, and so that's why we've just not--we proposed to not go forward with the

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formula.

GREENE, Q.C.:

Q. With respect to another proposal of Mr. MacDonald you did not comment on it, the first recommendation, was that there should be a trigger that if the formula produced a material change of 100 basis points up or down, that that would be material enough that a general rate application should be triggered, do you agree with that recommendation? It would address the concern we talked about earlier if the capital market conditions change so that the ROE should be reduced.

MS. PERRY:

A. I suspect that it's quite possible we would be in or called in before that 100 basis point should occur, but I don't have any principle problem, I guess with that 100 basis points.

GREENE, Q.C.:

Q. Do you agree with the 100 basis points or do you think it should be lower, say 50 or 75 basis points?

MS. PERRY:

A. I think given that I'm not convinced that a

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formula is actually the way to proceed in terms of estimating the cost of capital, I haven't actually put my mind around that if the formula were to proceed, would the 100 make sense or would the 75 make sense, I haven't really done that full analysis.

GREENE, Q.C.:

Q. If the Board were to determine that a--accept Newfoundland Power's position and that a formula would not be used to determine the fair return on equity and between rate cases, how about if there was--if the formula was used to determine whether a rate case should be triggered? You have mentioned before the Board could at any time, if the capital market conditions change, so the ROE reduces, they could ask Newfoundland Power to come in, would it give Newfoundland Power a level of comfort if there were parameters around when that would occur, such as a trigger of 100 basis points? So don't use it to set your ROE, use it to determine whether there's a rate case triggered.

MS. PERRY:

A. I think certainly that if there was a material

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change in utility's cost of capital and there was 100 basis points change, which I would consider material, that having a trigger to consider a rate case could be plausible. I'm just trying to think, I guess, of a situation where it's logical that let's say the cost of equity is increasing and it has increased across the country in that would we ever be in a situation where we're having to file cost of capital when there's no real concern that Newfoundland Power's cost of capital is out of step, so given I'm not sure what the formula would produce, I'm just not sure that we would or would not be out of step with appropriate cost of equities.

GREENE, Q.C.:

Q. And I guess we're not concerned so much about the cost of equity, the markets indicating an increase because obviously the utility then probably would be back looking for the increase. The concern would be if the cost of equity is actually declining in the marketplace and a formula would indicate that your ROE should be lower than what was last allowed, do you think a trigger then would be

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helpful or that you would know when the Board would expect you to come back?

MS. PERRY:

A. So I understand the question, so if Newfoundland Power's ROE were to decline by 100 basis points from where it's set, then that would be a trigger upon which Newfoundland Power would have to come in a file a rate case.

GREENE, Q.C.:

Q. Assuming that everything else remains the same.

MS. PERRY:

A. I suspect that would not be problematic, yes.

(2:00 p.m.)

GREENE, Q.C.:

Q. With respect to if there is to be a formula and I asked you about the deadband of the 25 basis points, you said it wasn't that that you disagree with. So do you accept that there should be a range where there is no change unless there is what I will call a material change in the ROE and is 25 basis points that correct materiality level?

MS. PERRY:

A. If I could explain the situation today or based on the previous formula, where we're actually regulated by rate of return on rate base, the way the formula operates today is that our return on the forecast cost of equity can change. That's then applied to the range of return on rate base and unless we fall outside the range of return on rate base, there may or may not be a change in customer rates because of the change in the cost of equity. So today we currently do have that deadband within the range of return on rate base. So certainly not against the -

GREENE, Q.C.:

Q. So there is a materiality trigger I will call it that you would agree with?

MS. PERRY:

A. Yeah, and I believe it's around 37 basis points today.

GREENE, Q.C.:

Q. Okay. Sorry, I'm getting a question from the back of the room with -- again, I'll ask -- the question is phrased in terms of "if there is no formula on a go-forward basis so the Board accepts Newfoundland Power's application in that regard and the market rates were declining, would regulatory lag be a problem for the Board?"

MS. PERRY:

A. Can you repeat that, Ms. Greene? Sorry.

GREENE, Q.C.:

Q. We're talking about the situation where we will have no formula on a go-forward basis and we're talking about when the market rates are declining, wouldn't a regulatory lag be a problem for the Board if we don't have a formula? That by the time that the Board actually determined that you would come in, there would be a lag because -

MS. PERRY:

A. Yeah, I -

GREENE, Q.C.:

Q. It's a question of the lag and the impact that has.

MS. PERRY:

A. I think that would exist today. If we were to base the formula upon a consensus forecast in November, as we do today, by the time we get to November, as we did in 2012, we were subject to regulatory lag because by the time we filed and by the time we received the order, we were midway through 2012. So if we had a formula that produced an unfair return or a formula that precipitated a change, it's probably not a lot different than where we are today.

GREENE, Q.C.:

Q. So you don't see a difference in the timing?

MS. PERRY:

A. Not right now I don't, no.

GREENE, Q.C.:

Q. Okay. Moving on to another topic which is deferral accounts. You are proposing in this application a number of deferral accounts that have a three-year recovery period and I won't go through each of those, but they're clearly laid out in your application. So with a three-year recovery rate, they will generally be recovered at the end of 2015. Is that correct?

MS. PERRY:

A. That is correct, yes.

GREENE, Q.C.:

Q. So if Newfoundland Power doesn't file a general rate proceeding to address rates for 2015, what happens with the amount that's now included in the revenue requirement to recover the amounts required for those deferral accounts?

MS. PERRY:

A. Well, I think anytime where we're amortizing certain accounts, a part of how we -- or when we determine the amortization period, the proposed amortization period, we do look at the impact that that's going to have on us over a certain period of time because it wouldn't be very strategic to amortize it all in one year and then the next year be left with a significant revenue shortfall or in the opposite direction. So when I look at CA-NP-398, which is our five-year forecast, the deferrals are obviously included in that forecast that we presented and when you look out to 2016, we're currently estimating an over seven million dollar shortfall.

GREENE, Q.C.:

Q. Would you like to bring that up?

MS. PERRY:

A. We certainly can, yes. 7.6 million dollar shortfall. And so even with those deferrals

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included in the revenue requirement, Newfoundland Power is projecting a 7.6 million dollar shortfall. So while that's in revenue requirement, we are obviously experiencing some other cost increases because that's just one of our costs, and in total, we're in a shortfall position. So without the deferrals, the amortization of the deferrals included in rates, that shortfall would be larger than that. So I think, again as we get closer to the '15 and '16, we will be making those observations about whether or not we can actually guide our way through '15, but it's looking highly likely that we will be in here for '16.

GREENE, Q.C.:

Q. So if you're not back in '16, what happens is you will still be collecting from customers the amounts that are included in your test year revenue requirement for the deferral accounts and it will part of the mix and used to offset other increases in costs because you will have already recovered what you should have recovered for those costs, such as the hearing cost, for example? Is that correct?

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MS. PERRY:

A. And that's a fair observation, and that's certainly consistent with how previous amortizations have been included in the past, from past rate orders, yes.

GREENE, Q.C.:

Q. Have you considered whether there should be some form of mechanism or process put in place to deal with the closure of deferral accounts other than a general rate application?

MS. PERRY:

A. No, and the biggest reason is I believe the shortfall that we're actually looking at, it's one of many of our costs and right now it looks as if we're not going to be in a position to have the opportunity to earn our return, so no, we didn't bring forward any proposal with respect to the end of the amortization period, those deferrals. And I do believe that it's worthy for the Board to consider the impact of the end of the amortization period, but in the context of what we're looking at on CA-NP-398, I think it's -- that it's fair that Newfoundland Power's costs are increasing and that even

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with the expiring of those amortizations, we're still in a revenue shortfall position. I certainly think it's a consideration of the Board.

GREENE, Q.C.:

Q. I wanted to next touch briefly on credit metrics. I did have some questions that have been addressed by Mr. Johnson and again, just to summarize what I understand your position is with Mr. Johnson. I believe you acknowledge that with both the proposed rates for 2013 and '14 and your existing rates, you would be within the range established and he took you through the Moody's range with respect to debt ratings. Is that correct?

MS. PERRY:

A. Yes, that is correct.

GREENE, Q.C.:

Q. I believe you indicated you would be at the low end of the range, but still within the range that Moody's has allowed for your current credit rating. Is that correct? So it's unlikely you would be downgraded?

MS. PERRY:

A. So sorry, Ms. Greene, and that's for which

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particular year?

GREENE, Q.C.:

Q. When you look at the current existing rates, which has incorporated 8.38 percent, and then your proposed, particularly 2012, 2013 and even Mr. Johnson took you to 2014. We can take -- call up your Exhibit 3, if you like.

MS. PERRY:

A. Yeah. No, I will agree that on Exhibit 3, if we could go to Exhibit 3, and looking at 2012, which is our current -- was that the question, Ms. Greene, the 2012 or is it 2013?

GREENE, Q.C.:

Q. It's also actually '13 and '14.

MS. PERRY:

A. Oh, '13 and '14.

GREENE, Q.C.:

Q. I understand where Mr. Johnson and you had a discussion that you also -- that you acknowledge that even for '13 and '14, you're pretty much still within the range, albeit at the low end of the range with respect to the existing rates?

MS. PERRY:

A. So in terms of what Moody's has indicated that supports the rating is a CFO to interest, which is on line 38, of low three times. So we're at three. And then the CFO to debt of 15 to 17. So we're actually below on that one metric.

GREENE, Q.C.:

Q. And I believe Mr. Johnson took you to where they said low teens and there was a discussion as to whether 13 was a low teen.

MS. PERRY:

A. Fair.

GREENE, Q.C.:

Q. And what my question is: you expressed a concern about what it meant to be at the low end of the range, and I wanted you to explain what is the significance for you and why it is of concern to you. If you're still within the range, why are you concerned that you are at the low end of the range?

(2:15 p.m.)

MS. PERRY:

A. So when you look at the metrics, Moody's has indicated that we are already lower than our peers and to support the metrics -- to support the credit rating, sorry, it's low threes.

We're at three. And it's between 15 and 17 and we're actually below. So in terms of the ranges that they've indicated to support the rating, we're moving one side. We're very close to the bottom. But that's combined with the fact that Newfoundland Power is, in this instance, earning a regulated return on equity of 6.89 percent. So, I look at metrics, but then I look at other observations of the Board, which I would have to then relay to the credit rating agencies, and I look at this situation of saying is earning a 6.89 percent allowed return on equity something that will precipitate a reevaluation by Moody's about the regulatory support in this jurisdiction, given that the 6.89 is considerably below -- considerably below the returns in Canada in particular.

So that combined with the metrics, I mean, failing metrics, declining metrics are not something that you want to be coming out of a general rate proceeding with. You know, when we left here the last time, in 2009 for 2010, these metrics were more like the interest coverage which is on line 37, 2.4,

2.5 range. The CFO to interest was at 3.4 and the CFO to debt was at 17.6. And so to be showing some things -- and those are within the range as indicated by Moody's for this rating. So to be declining metrics with a 6.89 percent regulated return on equity, I would have concerns that they would view that as a reason to reevaluate our credit.

GREENE, Q.C.:

Q. Why do you use credit metrics? I probably should have started with that question first. Why do we talk about credit metrics?

MS. PERRY:

A. So bond holders or credit rating agencies are trying to understand and display the risk for a bond holder. So cash flows seem to be the trump with respect to how much cash flows are available to pay the fixed cost of the utility, and so credit rating agencies apply credit metrics as guidance where companies should be for certain ratings. DBRS are not as specific as Moody's, but even DBRS will monitor and report our credit metrics, because I think it's the financial benchmark as to how we are compared to others, to display the

amount of cash flow we have to cover off the interest costs. So they're important because they're important to the debt rating agencies.

GREENE, Q.C.:

Q. And they measure your financial performance which is then used by the credit rating agencies to determine what your credit rating is for debt?

MS. PERRY:

A. Yes, absolutely.

GREENE, Q.C.:

Q. Okay. The last area of questioning relate to a couple of -- well, first, a regulatory reporting matter. Right now, Newfoundland Power files annually a curtailable service option report and a conservation demand management report as part of the requirements coming from Order No. P.U. 7 from 1996 to 1997. Is that correct, Ms. Perry?

MS. PERRY:

A. That is correct, yes.

GREENE, Q.C.:

Q. Does Newfoundland Power see any regulatory efficiency with respect to combining both of those reports into one report under

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conservation demand management?
MS. PERRY:
A. Yes, I would say that that would be in the direction of regulatory efficiency and we've looked at that and we would have no problem with combining those two reports.
GREENE, Q.C.:
Q. The last topic that I wanted to speak about is with respect to the rural subsidy and perhaps -- or rural deficit. I wonder if you could indicate or first explain to people what is the rural subsidy or rural deficit?
MS. PERRY:
A. Well, certainly the rural deficit is not new and not totally unique to Newfoundland, but it substantially refers to the cost of providing electricity to the more remote places on the Island and the cost to provide that electricity is out of sync with the revenue that you're getting from those remote areas. And I believe there was certainly substantial discussions and even a rural rate review as to the appropriateness of how this subsidy should be handled or this deficit should be handled. Should it be handled via the government

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through a subsidy or would it be included in Newfoundland Power's rates and that there would be uniform rates across the Island, for the most part. And from my reading as to what happened back in 1995 and onwards is that ship has sailed with respect to government policy with respect to the shortfalls that we're seeing in those areas, which are the isolated communities in Newfoundland, the interconnected for Newfoundland, the isolated in Labrador and I believe is L'ance au Loup.
GREENE, Q.C.
Q. Okay. So, the Board ask an RFI on this and I was wondering if we could bring up PUB NP 49. So, these are customers of Newfoundland Hydro -
MS. PERRY:
A. Yes.
GREENE, Q.C.
Q. - that do not pay the full cost of service, and that shortfall or subsidy is in, as a matter of policy, paid for by all other customers, is that correct?
MS. PERRY:
A. That is correct, yes.

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GREENE, Q.C.
Q. And -
MS. PERRY:
A. Sorry, it's not paid by the Industrial Customers of Newfoundland Power's customers, yes.
GREENE, Q.C.
Q. I'm sorry, right, Newfoundland Power's customers. And you include that as part of your revenue requirement to recover from your customers, is that correct.
MS. PERRY:
A. Yes, that is correct.
GREENE, Q.C.
Q. I wonder if we could scroll up to see the question, please. So, the question referred to the cost of service study that had been filed which was a 2011 cost of service study and the question was to provide a table showing the percentage of revenued derived from each customer class in 2011 attributable to the rural subsidy and forecast for 13 and 14. When you look down to the answer, first I wanted you to confirm that what was used for the table was what was used in Hydro's 2007

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test year which was the last test year that we have for Hydro and at that time it was 36 million dollars, is that correct?
MS. PERRY:
A. That is correct, yes.
GREENE, Q.C.
Q. So, assuming that forecast for the rural subsidy, the answer there is that based on that subsidy requirement of 36 million dollars, the percentage of your revenue requirement for 2013 is approximately 6. 1 percent for a domestic customer, is that correct?
MS. PERRY:
A. Yes, that is correct.
GREENE, Q.C.
Q. Okay. Are you familiar with Hydro's current forecast for the rural subsidy?
MS. PERRY:
A. Yes, I am.
GREENE, Q.C.
Q. And would you be able to tell the Board what the subsidy was for 2011?
MS. PERRY:
A. In total the subsidy for 2011 was 49 million

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of which Newfoundland power pays around 90 percent of the deficit; Labrador Interconnected pays the remaining ten. And my understanding is from that report that was filed in April by Hydro that the rural deficit is rising to 66 million in 2013.

GREENE, Q.C.:

Q. So, if Hydro were to file a rate case in 2013 with a two thousand (sic.) test year, the amount of the rural subsidy would be 66 million, based on the forecast that they have filed.

MS. PERRY:

A. We take about 90 percent of that, so around 60 million and that 60 million would translate into around 8.5 percent of our rates.

GREENE, Q.C.

Q. And you would pass that on when you do your flow through through the energy supply costs after Hdyro's rate case, is that correct?

MS. PERRY:

A. Yes, that is correct.

GREENE, Q.C.

Q. And you just mentioned, I believe, that that roughly then would increase the percentage of

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a domestic customer from the 6.1 percent to 8.5 percent, is that correct?

MS. PERRY:

A. Yes, the 6.1 percent here is based on 2011 revenues. So that 6.1, if you were to convert that into 2013's proposed revenue, it is around 5 percent because revenue is higher, so the percentage of the deficit to the revenue is lower. So, for comparing like for like, it's basically from five to about 8 1/ 2 percent.

GREENE, Q.C.

Q. Okay. And those conclude my questions for Ms. Perry. Thank you, Ms. Perry.

MS. PERRY:

A. Thank you.

CHAIRMAN:

Q. So, any questions here? Yes, we're going to hold off until you finish off tomorrow, Mr. Johnson.

MR. JOHNSON:

Q. Sure.

CHAIRMAN:

Q. So, we're back at 9:00 now, are we? Okay, we'll adjourn.

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Upon conclusion at 2:25 p.m.

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CERTIFICATE

I, Judy Moss, do hereby that the foregoing is a true and correct transcript of a hearing in the matter of Newfoundland Power Inc.'s General Rate Application heard on the 15th day of January, 2013 at the offices of the Board of Commissioners of Public Utilities, St. John's, Newfoundland and Labrador and was transcribed by me to the best of my ability by means of a sound apparatus.

Dated at St. John's, NL this
14th day of January, 2013
Judy Moss
Discoveries Unlimited Inc.

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